S. HRG. 100-373

REPORT BY THE GENERAL ACCOUNTING OFFICE ON ARMS EXPORT LICENSING AT THE DEPARTMENT OF STATE

HEARING

BEFORE THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

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REPORT BY THE GENERAL ACCOUNTING OFFICE ON ARMS EXPORT LICENSING AT THE DEPARTMENT OF STATE

FRIDAY, SEPTEMBER 11, 1987

U.S. SENATE,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Committee met, pursuant to notice, at 10:05 a.m., in room SD-342, Dirksen Senate Office Building, Hon. John Glenn, Chairman of the Committee, presiding.

Present: Senators Glenn, Pryor, Stevens, Roth, and Sasser.

OPENING STATEMENT OF CHAIRMAN GLENN

Chairman GLENN. The hearing will be in order.

This morning we will be hearing testimony from several witnesses on the Federal licensing procedures for arms exports.

Before I continue with my brief remarks I would like to commend Senator Pryor for the very excellent work that he has presented to this Committee in February of this year and the work he has done on the same issue throughout this year.

We look forward to very carefully reviewing the results of today's hearings. That this is a mounting problem is evidenced by some of the charts over here that you have probably already looked at and that David will be using later on, I am sure.

The previous testimony that we have had has focused on the capabilities and competence of the Office of Munitions Control [OMC], the office in the State Department with primary responsibility for reviewing and issuing arms export licenses.

The evidence showed that applicants have relatively easy access to obtaining licenses to export arms. OMC's lack of export control during a period from 1977 to 1986 has allowed marked increases in arms exports. What we are going to deal with is whether this has been justified or not and what the procedures are.

As a result, it is clear that American weapons technology is being increasingly transferred abroad. Now, that can be good or it can be bad. It is one of the things to be looked into. Possession of this technology allows foreign industries to not only better compete with American arms manufacturers for sales to friendly countries, but it raises the risk of weapons technology transfer to unfriendly countries as well.

The Committee asked GAO to review this whole process.[1] They were asked to review the Office of Munitions Control license review process. Today we will hear important testimony from GAO concerning its recommendations that OMC strengthen that process. At a minimum, OMC must be more diligent in its efforts to screen applicants for these licenses. For instance, information about previous violations or questionable applications must be gathered and considered.

In my view, it is imperative that all offices involved in enforcing arms licensing laws—including OMC, the U.S. Customs Service, the Commerce Department, Defense Security Assistance Agency—all effectively work together and share critical information.

Senator Pryor, I look forward to hearing the testimony and your recommendations. I will review it in its entirety. I cannot be here for all of today's meeting because I have some other commitments, but I wanted to be here and make sure that my interest as Chairman was shown in this because it is of tremendous interest to me. We have been very much concerned about some of the technology transfer as well as just the gross numbers of arms and weapons systems being sent abroad.

I am particularly glad of the lead that you have taken in this particular area. And the GAO report, we look forward to getting information on that today.

Senator Stevens, do you have any opening statement?

Senator STEVENS. No. I am here at Senator Roth's request. He will be here soon. I, too, am very interested in this, Mr. Chairman, and I look forward to the statement of Senator Pryor. I do hope that we can get into the question of the adequacy of the verification of the statements made by applicants and whether or not there is a post-approval inspection program that is adequate.

Chairman GLENN. Thank you. David?

OPENING STATEMENT OF SENATOR PRYOR

Senator PRYOR. Mr. Chairman, I want to thank you this morning for agreeing to hold this very important hearing on the results of the arms export study that I requested several months ago from the General Accounting Office. Mr. Chairman, some people may disagree with me, but I see nothing wrong with the prudent sale of U.S. military hardware abroad.

The real issue is, what are we exporting and where do the arms we export end up? We have been learning the hard way that a sophisticated black market for American military parts and munitions efficiently supplies many of our potential adversaries, from Iran to North Korea.

We must ask ourselves now how the black market eludes our security controls on arms sales and exports. Where are the weaknesses and holes in that system?

Mr. Chairman, I think that the weakest link may be our free and open borders. The Customs Service, for example, stopped almost 400 illegal arms exports last year, but they freely admit they can only stop a trickle of the flow. Another weakness appears to be in

[1] See GAO report on p. 59.

our military supply and disposal program. But the most overlooked weakness that we have in the system today and the one most susceptible to corrective action appears to be the Office of Munitions Control, or OMC, the State Department's arms export licensing office.

This hearing, Mr. Chairman, is not about the Foreign Military Sales Program. That is handled by the Defense Department. These are commercial arms sales that we want to talk about this morning and how those potential exporters apply and receive their licenses to export arms abroad. When I chaired a hearing of this Committee on arms transfer policy last February, the Director of OMC had a very shocking story to tell. Over 10 years, workload has doubled to $14.9 billion of arms exports a year, but the tiny staff of 30 had not grown.

There are five licensing officers who review almost 50,000 license applications a year. They had no procedures manual and only minimal computer support. As for law enforcement, Mr. Chairman, OMC had not debarred a company in 4 years, OMC had no computer link with any intelligence or law enforcement database, OMC did not maintain a list of potential export criminals, and the head of compliance said he would not take action against most criminals, even if they were identified.

After that hearing I asked GAO to perform an investigative audit of OMC. The findings we will hear about this morning indicate that OMC is either incapable or is negligent in most of its areas of responsibility: registration of exporters, licensing, enforcement, agents fee reporting, and verification of end use.

GAO reports that one study found, "negative information," on 26 percent of a sample of those registered at the State Department and 27 percent of export consignees. In all fairness, some negative information does not necessarily impeach the intent or character of all the identified companies or individuals. But if OMC does not check such things, how are we to know who is licensed to sell American arms abroad.

GAO also reports that OMC gave 322 licenses to a company while it was denied export privileges at the Commerce Department. The Commerce Department has been criticized for being too easy on questionable exporters. What does that say about our own State Department?

In January, 1987, two former principals in that same company were named in a 27-count indictment for violation of the Trading with the Enemy Act and the False Statements Act. This company today continues to get arms licenses at the State Department through the Office of Munitions Control.

Shocking? Yes. This is only the beginning, Mr. Chairman.

Just over a year ago Armoflex, Inc., was named in an indictment for the sale of aircraft and parts bound for where? Bound for Libya. Three days after its indictment, Armoflex received an OMC license to export tank parts. Two months later this same company received other similar licenses, once again for the sale of tank parts.

In 1984 a company called American Aviation Parts plead guilty to the sale of military aircraft parts to Chile, a country embargoed

by the United States. Since its guilty plea they have received 65 arms exports licenses from our own State Department, OMC.

How could things decay so quickly? Has not anyone sounded an alarm at the State Department?

Well, some people have. In a 1985 memorandum on problems at OMC, a disturbed official warned his superiors, "We must act now, before it is too late."

In an earlier report, the head of OMC said their computer system, "seriously threatens an embarrassment of our enforcement capabilities." Even this threat of embarrassment or danger to national security went unheeded by the top echelon of our own State Department.

Since our hearing last February, Mr. Chairman, many people have volunteered comments about the history of problems at OMC. The commercial arms exporters who spoke to me commented on slow and inconsistent license review, sloppy procedures, too little staff, ancient computers, and no innovation. They even told me they were frightened by OMC's inability to screen illegal exports—frightened because most exporters have a good reputation to worry about.

One exporter said that, compared to its counterparts at Defense and Commerce Departments, the Office of Munitions Control is still in the 19th century. Most observers do seem to agree that the licensing office is already in trouble and is now headed for disaster. As the OMC official said, "We must act now before it is too late."

Some say OMC should be moved to the Department of the Treasury, or to the Defense Department, or even to the Department of Commerce. Surely one of them would take this $15 billion a year job more seriously.

I have looked into those options, Mr. Chairman, and for the life of me, I cannot decide where OMC should be. I guess at this moment I am saying it should remain at the State Department, but only—and I underscore only—if drastic changes can be made. GAO identifies actions that OMC and the State Department must take, and I intend to introduce legislation describing actions that Congress must take.

Mr. Chairman, on a personal note, I would like to commend the General Accounting Office and the very splendid staff that has worked on what I believe to be one of the finest reports that I have ever seen from the General Accounting Office. This report has exposed a scandalous situation in the Executive Branch of our Government, and I think, too, it has offered a blueprint that the Congress must follow in the future to correct this situation. It is now up to the Congress and the Administration to work together to forge a lasting solution.

Mr. Chairman, that is the end of my opening statement, and I wonder if Senator Stevens or yourself will have a statement before we have our first witness?

Chairman GLENN. Senator Heinz, who could not be here, has a statement for the record which will be included at this point.

[Senator Heinz' statement follows:]

OPENING STATEMENT OF SENATOR JOHN HEINZ

Mr. Chairman, the issue we address here today does not grab many headlines, but it goes to the heart of many American foreign policy and national security concerns. The United States defense sector is a strong, innovative, and successful exporter. The Office of Munitions Control was established to make sure that U.S. arms exports conform with U.S. foreign policy interests, as expressed in laws passed by Congress and decisions made by the Executive Branch.

From the GAO findings we are discussing today, it appears that due to underfunding and mismanagement, the Office of Munitions Control is unable to give us confidence that its mission is being fulfilled. If we could safely assume that no one in the defense industry would export contrary to U.S. law or policy, this would be of little concern. Unfortunately, recent history contains too many examples to show this is not the case.

In the last ten years, the number of cases processed by the Office of Munitions Control has nearly doubled to almost 50,000 per year. Yet the Office's staff has remained the same size—five staffers to review all those applications. In the last decade only four exporters have been debarred for violating U.S. laws. And even some exporters debarred by other agencies such as the Commerce Department are allowed to export by the State Department. To some observers, it might seem that American private arms exports are simply not under meaningful control of the U.S. Government.

This is a serious situation. The case for significant action seems to have been made. What we need now are some guidelines for remedial steps that Congress and the Executive Branch can work out together. I thank the witnesses for appearing, and I look forward to their views of where we go from here.

Senator PRYOR. I also have a statement by Senator George Mitchell of Maine that I would like entered into the record at the appropriate point. He did participate in our February hearing and I must say asked a series of very splendid questions.

[Senator Mitchell's statement follows:]

OPENING STATEMENT OF SENATOR MITCHELL

Earlier this year, at the Committee's February hearing, I observed that the question of American arms sales abroad involves a range of sensitive, complex issues. They include issues of American foreign policy; regional balances of power; collective security; human rights; and undeniably, the financial interests of American arms manufacturers.

The recent Iran Affair dramatically illustrated the significance which transfers of arms can have on the world stage.

In February, I also noted that there is a fundamental, underlying moral issue—which unfortunately sometimes is lost in the complexities of issues, and in the technical details of the arms export licensing bureaucracy.

The world is awash with weapons of violence and destruction. Too often, individuals and nations resort to force of arms to settle disputes or make political points. And the United States must bear some moral responsibility for that fact.

I also observed earlier this year that the central question which concerned the Committee—in trying at least to regulate the flow of arms, for which we bear some responsibility—is whether or not the arms export licensing system is working.

Frankly, I was troubled by the answers provided to the Committee earlier this year by the Director of the State Department's Office of Munitions Control (OMC), which were like a blank stare in the face of the challenge of responsibility.

And I am shocked today by the results of the General Accounting Office's Report on its review of OMC procedures and operations:

OMC "does not verify the accuracy of information provided by registrants."

OMC does not systematically check applicants against "lists of questionable exporters, exporters convicted of past export violations, or those denied export privileges by the Department of Commerce."

OMC issued 322 licenses, worth $15 million, in FY1986 to a company denied export privileges by the Department of Commerce.

OMC has the power to revoke licenses, but has done so in only four instances since 1976.

Obviously, the system is not working.

And it is the Committee's responsibility to see that it fixed; and that those who are given responsibility within the arms export licensing system, exercise it efficiently and effectively.

Senator PRYOR. Mr. Chairman and Senator Stevens, our first witness this morning is Ms. Joan McCabe, the Associate Director of the National Security and International Affairs Division of the General Accounting Office. She is accompanied by Mr. Barry Holman, Mr. Albert Huntington and Ms. Margaret Gaddy.

As a result of a Governmental Affairs Committee hearing last February that we have already alluded to, I asked the GAO to review the operations and the procedures of OMC, the Office of Munitions Control, within the State Department. As I have said before, this is a splendid report. It is hard hitting. It is also clean. I think it is very fair. Certainly it is educational and illuminating. I commend the General Accounting Office.

Ms. McCabe, I want to thank you for coming today and for bringing your staff. You will have about 10 minutes or so for your oral testimony, after which Senators will be given time for questions.

TESTIMONY OF JOAN M. McCABE, ASSOCIATE DIRECTOR, SECURITY AND INTERNATIONAL RELATIONS, NATIONAL SECURITY AND INTERNATIONAL AFFAIRS DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY ALBERT HUNTINGTON, GROUP DIRECTOR, AND MARGARET GADDY AND BARRY HOLMAN, EVALUATORS

Ms. MCCABE. Thank you very much, Senator Pryor.

Mr. Chairman, members of the Committee: We are pleased to be here today to discuss our recent review of the Office of Munitions Control (OMC). I have a very detailed statement that I would like to submit for the record and what I will do now is summarize or highlight that statement.[1]

The results of our review are contained in our report which I understand is being released today. That report identifies a number of areas where OMC can improve its licensing operation. For example, OMC could make better use of readily available information. Agencies such as Commerce, Customs, Justice, and Defense (DOD) have information on exporters convicted of violating export laws and regulations, on those denied export privileges, and other engaged in a wide range of questionable activities. But OMC does not check its license applicants against these information sources. As a result, at times OMC has approved licenses for parties barred by other Federal agencies.

In our report we are recommending that OMC use available information from other Federal agencies to identify license applications needing closer scrutiny. In other words, OMC should use this information to flag cases requiring more indepth review. In a related vein, we found that OMC does not verify or test information submitted by applicants for accuracy or veracity. According to OMC officials, they simply lack the resources to do so.

One way to verify information is to ask the U.S. Embassy in the destination country to check to see whether the transaction ap-

[1] See p. 37.

pears legitimate, but OMC rarely does this. Of the approximately 49,000 license applications OMC received in fiscal year 1986, only about 50 were sent to U.S. Embassies for end-use checks. We think U.S. Embassies could be tasked more frequently to provide these checks and are recommending OMC develop guidelines to facilitate these efforts. Doing so should not required any large increase in resources yet would provide greater assurance that license application data is accurate and that the proposed sale is legitimate.

Another area ripe for improvement is OMC's capabilities to store and retrieve data. Presently, OMC's facilities for data storage and its automated data processing capabilities are insufficient to meet its needs. Increased automation would greatly improve license reviews. OMC is addressing its immediate data processing needs but has not assessed its long-term needs. We are recommending that OMC conduct such an assessment with a view toward automating much of the export license review process.

Lastly, we found that some regulatory requirements are slipping through the cracks. For example, certain export license applications are supposed to have a statement identifying whether political contributions and agents fees were paid in connection with the sale. In our sample we could not locate about 40 percent of the statements that should have been there. OMC needs to take steps to ensure that exporters comply with this and other administrative requirements.

OMC officials told us that its increased workload and the static resources have limited the time they can devote to license reviews and have restricted their ability to ensure compliance with all administrative requirements. OMC's volume of munitions cases has increased from 26,000 in 1977 to over 49,000 in 1986 and is expected to exceed 52,000 in 1987. Over the same period, OMC's staff has remained, as you noted earlier, at around 30 with 10 staff members authorized to review licenses.

We recognize that budget limitations have imposed constraints on OMC. We believe, however, that even within tight constraints, OMC can improve its operations by taking steps such as the ones we have recommended to better screen and review license applications.

This concludes my prepared remarks. I would be happy to answer any questions you might have.

Chairman GLENN. Let me ask just one question before I go.

Senator PRYOR. Sure.

Chairman GLENN. The people there—and I am sorry I cannot stay for the whole hearing this morning—but the people over there must realize the inadequacy of what they are doing. Is this a matter of budget? Have they been turned down on budget requests to expand their operation, to get more people to do a more thorough job in checking and following up on these things? Is that the major area? Are budget problems at the base of this?

Ms. MCCABE. OMC management has been concerned about the strain that has been imposed on the staff with the increase in their workload. It is very hard to find a paper trail on the budget requests—that is, who turned down what when. I think that might be a question addressed to the State Department because we are not

quite sure. We tried to get that information and could never find a good trail of requests and turndowns.

Chairman GLENN. Were you refused, or is there just not a record there?

Ms. MCCABE. I believe there was just not a good record of it.

Chairman GLENN. Well, somebody must certainly have tried to expand their operation there. You cannot have five reviewing officers and 49,000 requests in 1986—I believe you said in your statement—and think that anyone is doing an adequate job of checking the criteria there, the licensing criteria, the four or five different things that they have to look at. You could not read that many in a year.

Ms. MCCABE. OMC has developed a productivity plan that calls for increases in staff, for improved computer capability, and also for assigning military officers to OMC to help with the technical aspects.

A number of those recommendations are falling by the wayside due to budgetary constraints. We understand that the increase in staff that was proposed for 1988 has not gone through.

Chairman GLENN. OK. If I am making a widget and it is—whatever it is, it is a military thing that I want to sell—and if I go to State and I get a license, is there another stop along the way then? Do I then have to go to Commerce?

Ms. MCCABE. No; you do not.

Chairman GLENN. Once I have my licensing, I then can go sell my widget to whoever I want to sell it to or whatever the application was for?

Ms. MCCABE. If the widget is on the Munitions List and licensed by OMC, you would just have that one stop at OMC, unless OMC decided for some reason they wanted to send your application to the Department of Defense or ACDA or some other bureau within the State Department to get their opinion on it. In about 20 percent of the cases OMC will staff the license applications out to other agencies so that they can examine the applications from national security, technical and human rights perspectives.

Chairman GLENN. Well, thank you. I have no further questions. I just want to once again say to Senator Pryor, we appreciate very much your taking the initiative in looking into this. I think it is a very fertile field on this whole process, because the munitions sales have gone up tremendously and I think we want to follow through on this, the whole process.

Thank you for your initiative on this.

Senator PRYOR [presiding]. Thank you, Mr. Chairman.

Just to comment on a statement you made about munitions sales going up drastically, it appears to me in looking at foreign military sales versus the commercial sales—we are looking at the private sales now—the private sector has really risen much more rapid than the government-to-government sector, is this correct?

Ms. MCCABE. I do not have the exact numbers with me, but I believe government-to-government sales have actually gone down and the commercial sales have gone up.

Senator PRYOR. Has gone down and the commercial has gone up. Is that because there might be large fees and agents commissions attached to this, or the is bureaucracy easier to deal with?

Ms. McCABE. There is probably a number of reasons for why purchasers would opt to go commercial as opposed to government-to-government. One consideration may be whether one has FMS credits or grant financing. The FMS credit program has been contracting.

Also many licenses being granted by OMC are for spare parts, whereas the original sales of the major items may have gone government-to-government in the late 1970s or early 1980s. In other words you are now catching the spare parts trail. About 60 percent of the permanent export licenses cover spare parts.

Senator STEVENS. Could I get into that?

Senator PRYOR. Certainly.

Senator STEVENS. You are not suggesting, are you, that we would have to have a major congressional approval for all the spare parts that go out?

Ms. McCABE. No; I was just trying to explain why there may have been increases in commercial sales and decreases in government-to-government.

Senator STEVENS. Is GAO taking the position that the State Department's activities are defective because they do not, in effect, have a small FBI to investigate all of these applications?

Ms. McCABE. No, we certainly are not taking that position.

Senator STEVENS. Was that your recommendation to us?

Ms. McCABE. Our recommendation is that the State Department avail themselves of information that other agencies already have. Other agencies have already done the investigations or data gathering.

We believe State should routinely—when an exporter is registering or when an exporter is applying for a license—bounce those names against the available information from other agencies to determine which exporters require a closer look.

We are not saying that they ought to go out an investigate everyone. We are saying that information exists within the Federal Government that they should use.

Senator STEVENS. I am told that OMC authorized $12.7 billion in exports in 1984 and $3.8 billion were actually sold. Are those your figures?

Ms. McCABE. Those are OMC's figures, yes.

Senator STEVENS. With that statement of fact what is GAO's recommendation about the process by which the exports should be kept track of? Do you think there should be a monitoring process to see how much goes out, where it goes, who is involved in exporting them, whether they have been convicted of crimes?

Ms. McCABE. We think the best time for the State Department to get involved in this would be on the front end when OMC is either registering the exporters or when OMC is reviewing individual licenses. It would be very difficult for State to trace items after they have been sold.

The information might be most useful if you knew about it before you approved the license. We believe OMC should use readily available information to determine whether the particular applicant requires additional scrutiny.

Senator STEVENS. I have some problem about the whole process, but I have some problem about your report, too. It appears that

you want a preliminary screening and if the applicant and the application are all right, you would just forget about it. I think the other way around, that where the munitions go and who actually delivers them, who verifies that they went to Great Britain rather than to Iran, is much more important than who is involved in making the original application and explaining the type of process involved.

I have got to tell you, I think that the downstream verification is much more important that the preliminary verification.

Ms. McCABE. We appreciate your concern. We also have those concerns. The United States does not have a good system to track this type of information. Generally the U.S. Embassy in a given country do not know what is coming into that country. For example, our Embassy in London would not know what is being exported from the United States to the United Kingdom.

Senator STEVENS. Is the United Kingdom notified?

Ms. McCABE. If the United Kingdom was the purchaser it would be.

Senator STEVENS. If I were the purchaser in the United Kingdom, is the Government of the United Kingdom notified?

Ms. McCABE. I do not believe so. Now, if it were a particularly sensitive item or a significant military item, OMC could require the Government to execute a "nontransfer and use certificate" (DSP-83). The United Kingdom Government would be notified that the United States wants the Government to buy into our end-use rules. In other words, that the item may be transferred to a purchaser in the United Kingdom but, could not be transfered to another country without approval of the State Department.

Senator STEVENS. Thank you very much.

Senator PRYOR. Ms. McCabe, I think Senator Stevens has raised a good point and I think it is appropriate to just examine for a moment the very first contact that the OMC and the State Department has with a potential exporter. That very first contact, other than the possibility of a telephone call coming into the office that says where do we pick up the form, the license application, would actually be in this application.

It is form DSP-5, Department of State Use Only. I am going to have this submitted for the record at the appropriate place. Have you seen one of these forms?

Ms. McCABE. Yes, I have.

Senator PRYOR. On this form, is there any question that relates to or asks the applicant to state whether or not he or she has a past conviction or felony for treason, trading with the enemy, or anything of this nature?

Ms. McCABE. Not on that form, no.

Senator PRYOR. So on this application form there would be no indication, no red flag raised for OMC?

Ms. McCABE. No.

Senator PRYOR. Second, after looking at this form and actually driving into work this morning, it dawned on me that I did not think—and I reached in my briefcase to research it driving in and I almost had two car wrecks trying to find it—I do not believe it asks the person, the applicant, if he or she is an American citizen or

not. So the applicant does not have to be a citizen of this country; is that correct?

Ms. McCABE. Yes. It could be a foreign government.

Senator PRYOR. It could be a foreigner or a foreign government?

Ms. McCABE. Yes, a foreign entity.

Senator PRYOR. I would like to have this submitted at the appropriate place in the record and will do so.[1]

Now, we have a chart that also relates to some of the concerns that have been expressed this morning. I believe that chart is up here. It deals with several companies and individuals, perhaps, that have either been indicted or plead guilty or on probation or whatever, that are being awarded contracts today by the Office of Munitions Control.

For example, officials at Associated Industries—I mentioned this in my opening statement. They were indicted January 21, 1987—that was this year—pending trial. The charge, taking part in the illegal export of 85 Hughes helicopters to North Korea; a 27-count indictment.

Now the question, does OMC still grant the company the opportunity to do business?

Ms. McCABE. Yes.

Senator PRYOR. In fact, 124 occasions since the indictment, and it is my understanding that the Department of Commerce had denied them export licenses at one time.

Ms. McCABE. Associated Industries had been denied, yes.

Senator PRYOR. Now, my question is this, how can they continue to do business with this cloud of controversy? Is not there a red flagging system in OMC that would catch this?

Ms. McCABE. No.

Senator PRYOR. There is none?

Ms. McCABE. No, and this could happen because they do not have a process or a system within OMC whereby they would routinely check who was on these debarred lists. That is what we are recommending, that they get that information so they can consider it.

I think the comment you made earlier about the presence of adverse information not necessarily meaning that OMC erred in granting the license is correct. But it certainly would be the red flag that you are talking about. You would want to look closely at what was being shipped, where it was being shipped it to, and then to determine if there is any indications that items were being are diverted.

Senator PRYOR. Just for the record, I would like to state that there were two officials with Associated—I believe Ronald and Monte Semler—who actually were the ones indicted and not the company itself. But the point is that while the company was being denied export licenses at the Department of Commerce, it was still being granted licenses by the Department of State.

Ms. McCABE. During the period of our review we found that to be the case. Since our review ended I do not know if anything has

[1] See p. 56.

changed, but during the period of our review we found that they had granted this company over 300 licenses.

Senator PRYOR. Over 300 while they were under indictment?

Ms. MCCABE. While they were debarred by Commerce, or denied export privileges by Commerce.

Senator PRYOR. The allegation was violation of Trading with the Enemy Act, false statements, conspiracy and tax counts, and still doing business with OMC.

Well, the third company, I believe, on that list is Armoflex, Inc. They were indicted July 21, 1986, once again pending trial. Conspiracy to export and the export of two Lockheed aircraft and spare parts to Libya.

What has happened to that company? Are they still getting licenses with OMC to trade in arms?

Ms. MCCABE. Margaret, can you answer that?

Ms. GADDY. We do not know if they are presently getting them.

Senator PRYOR. I think the facts of that matter regarding Armoflex are: Date indicted, July 21, 1986; received an arms export license just before indictment on July 8 and again after indictment on July 24 and September 22, 1986. So it appears that the indictment did not raise any flag to OMC.

Ms. MCCABE. Again, during that time, no.

Senator PRYOR. That is my point. There are several other companies and organizations on that list. I will not go into each of those particular cases. I would ask that this list of companies who have been indicted or have plead guilty—well, here is one—Aeromarine International, indicted July 1985, a plea of guilty, October 1985, and still 10 licenses in 1986, a year later, to continue exporting arms to Chile and Argentina.

Ms. MCCABE. Yes.

Senator PRYOR. So that was the unlicensed export allegation to which they plead guilty.

This chart will be made part of the record.

[The information referred to follows:]

CONVICTED OR INDICATED COMPANIES LICENSED OR REGISTERED BY OMC

Company	Date indicted	Disposition	Charge	OMC licenses
U.S. v. Ronald and Monte Smeller (Associated Industries), trading with Enemy Act, false statement—comspiracy tax counts.	Jan. 21, 1987	Pending trial	Illegal Export of 85 Hughes Helicopters to North Korea. 27 count indicatment.	124 since indictment.
Rettig Electronics, U.S. v. Rettig Electronics, Inc., Arms Export Control Act.	March 1984	Plea and fine, March 1984.	Unlicensed export of night vision goggles and torpedo tube heaters to Chile.	1 on Sept. 25, 1985.
U.S. v. Edward J. Elkins, et al. (Armoflex, Inc.), Export Administration Act.	July 21, 1986	Pending trial	Conspiracy to export and the export of 2 Lockheed aircraft and spare parts to Libya.	3 in 1986: On July 8, 1986; July 24, 1986, Sept. 9, 1986.
Aeromarine International, U.S. v. EMGE Aeromarine International, Arms Export Control Act.	July 1985	Guilty Plea and Fine, October 1985.	Unlicensed export of military equipment to Chile and Argentina.	10 in 1985, 10 in 1986.

CONVICTED OR INDICATED COMPANIES LICENSED OR REGISTERED BY OMC—Continued

Company	Date indicted	Disposition	Charge	OMC licenses
U.S. v. Zacharia, et al. (Levy Auto Parts), Arms Export Control Act.	June 1982	Probation/fugitive	Conspiracy to export tank parts to Iran without a license.	28 in 1985–86, 37 in 1987.
American Aviation Parts, U.S. v. American Aviation Parts, Arms Export Control Act.	October 1984	Plea and fine, November 1984.	Unlicensed export of military aircraft parts to Chile.	35 in 1985, 17 in 1986, 13 in 1987.
Charlotte Aircraft, U.S. v. Charlotte Aircraft and Herman O. Brown.	April 1982	Plea and fine	Unlicensed export of inertial navigation systems to Libya.	Registered, no licenses.
Tencom Corp., U.S. v. Tencom Corp., et al.	July 1982	Fine	Unlawful export of aircraft and helicopter parts to Libya.	Do.

Note.—All licenses were received by referenced companies.

Sources: Department of Justice List of Significant Export Control Cases Office of Munitions Control records.

Senator PRYOR. So the basic bottom line is, OMC has no flagging device to identify these companies or these individuals.

Ms. MCCABE. Yes. OMC needs a system to identify which exporters require additional scrutiny before making a determination on granting a license.

Senator PRYOR. All right. Well let's say a red flag did go up on the computer, assuming it is archaic. Does OMC then have the basic legal authority to deny a license to a company that has been denied by the Department of Commerce or any other suspicious situation?

Ms. MCCABE. OMC has some very broad bases for denying licenses—national security, foreign policy, and certainly violations of the Arms Export Control Act.

Senator PRYOR. How many licenses have they denied?

Ms. MCCABE. In 1986 about two percent were denied. They approved about 90 percent. They also returned about eight percentage without action. I think out of about 49,000 applications, something like 800 were denied.

Senator PRYOR. So, 49,000 requests and 800 denials.

Ms. MCCABE. Yes, 800 were denied outright. Others were returned without action, which is in effect a denial. You could take the both figures together and say 10 percent.

Senator PRYOR. Is OMC plugged into the Department of Defense computer or into the Department of Commerce computer system so they can identify, let's say, suspicious characters or maybe people on the "bad guys" list?

Ms. MCCABE. No. Into the computer systems, no.

Senator PRYOR. Why is that? That would not be hard to do, would it?

Ms. MCCABE. No, it probably would not be hard to do. There may be some concerns about protecting data. Obviously there are some costs involved. We do not have a good idea why that has not happened. The subsequent witnesses might be able to help you there.

Senator PRYOR. In looking at OMC, do you think they would necessarily deny licenses to persons identified as having been denied by other agencies like Defense and Commerce. If they knew that

they had been denied by Commerce, then would OMC automatically deny them a license?

Ms. McCABE. No. I do not think they would automatically deny them the license, but I think that it would be a very valuable piece of information for them to have because then they would want to look much more deeply into what was being exported and where was it going. I would think that if you had a situation like that, you would automatically flag it for an Embassy end-use check before you would approve the license.

These other agencies have a lot of the information that ranges from the very serious to technical violations. OMC would have to evaluate just what the adverse information was and whether it had any real impact on the particular transaction under consideration.

Senator PRYOR. We have alluded to where some of these munitions, weapons or parts or whatever wind up. Where is the end use? What is the end user country?

My fear is that a lot of this winds up in the hands of terrorists or in Libya or in Iran or wherever the situation might be. How do we control that?

Ms. McCABE. That was well outside the scope of our current review and we do not have any good information on that. We do have information on what countries favor commercial sales versus government-to-government. Mr. Huntington can give you that information.

Senator PRYOR. Mr. Huntington?

Mr. HUNTINGTON. End-use checks, once the munitions item leaves the United States, have been pretty much left up to the intelligence community and members of U.S. Embassies in the respective countries. What we can highlight for you are those countries that have used the commercial military sales channels the most. We are relying on statistics that are published by Defense Securities Assistance Agency (DSAA) and that, as we state in our report, are probably understated. So rather than take the numbers as hard numbers, I think the trends are important.

We looked at what DSAA tabulated from 1950 through 1986. Japan and Israel accounted for 22 percent of what is reported over that period. The top 10 countries accounted for over 65 percent of what was reported as exported under commercial sales licenses.

Senator PRYOR. Now, these are the end-use countries?

Mr. HUNTINGTON. Yes, sir. That is correct, as stated on the license.

Ms. McCABE. Declared end-use countries.

Mr. HUNTINGTON. Those countries that were reported through OMC to DSAA for inclusion in its annual report. The point here is, though, a number of countries—10 countries—account for a very large percentage of what is exported overseas.

Senator PRYOR. What is the largest?

Mr. HUNTINGTON. Japan and Israel accounted for approximately 10 to 12 percent each over the period 1950–86. I also looked at 1984, just as a possible year where perhaps the exports had been completed, since most licenses are good for 2 years. It turns out, coincidentally, that Japan and Israel are also the top two from fiscal year 1984.

But other countries in 1984 that were large purchasers through the commercial sales channels include Saudi Arabia, the United Kingdom, Belgium, Canada, Germany, Taiwan, Korea and Australia. Most of these nations are NATO nations or favored nations with the United States.

We are not suggesting that there is any question or problem here. It is just that they account for a very large percentage of the commercial sales. But on the other hand, in 1984 approximately 140 countries bought through commercial channels. These ranged from very small amounts to the very high amounts that Israel, Japan and some of the others that I read off purchased.

Senator PRYOR. How many checks did you say, or did this GAO report maintain, that were made from the 49,000 or 50,000 sales? How many checks to see where these weapons or supplies wound up?

Ms. MCCABE. Only 50.

Senator PRYOR. Fifty out of the 50,000?

Ms. MCCABE. Yes, approximately. We got that number from discussions with OMC officials. OMC does not maintain a record on all end-use checks that have been done in any given year.

Senator PRYOR. So this would come under the enforcement division of OMC?

Ms. MCCABE. Yes, its compliance section.

Senator PRYOR. How many individuals are in the enforcement division of the Office of Munitions Control?

Ms. MCCABE. The area that does OMC's compliance work consists of a manager and two paralegals.

Senator PRYOR. Three people?

Ms. MCCABE. That is what it was during the course of our review.

Senator PRYOR. To do the enforcement on 50,000 sales?

Ms. MCCABE. Yes.

Senator PRYOR. A manager and two paralegals? Where has the State Department hierarchy been all these years? What does the Secretary of State say about how this was allowed to happen?

Ms. MCCABE. I would not presume to speak for the Secretary of State.

Senator PRYOR. If this were not so serious it would be almost a comedy, but it is a tragic, tragic comedy.

Senator Stevens may have some questions at this point. I will have more later.

Also, we have been joined by a member of our Committee, Senator Sasser of Tennessee. Senator Stevens?

Senator STEVENS. Well, Mr. Chairman, I do have to leave and I do not have any questions. I do have a statement to make, though. I am not so sure it is this serious. It does seem to me that the current situation warrants some consideration of who ought to be following up, but I do not want to see another bureaucracy in the State Department and the implication here is that we should build a little FBI to have further enforcement in the State Department.

Beyond that, the overwhelming bulk of these people are our very good allies—Japan, Israel, Britain. Are we suggesting that because there might have been someone previously convicted of some crime

who handled a shipment to Israel, that there is something wrong with it, Ms. McCabe?

Ms. McCABE. No, we are not.

Senator STEVENS. Well, the implication is here that, my God, all of these sales went out of this country and isn't this terrible. I would much rather see these sales going from the United States than from Cuba or Nicaragua or some of the places in this world that could break ties with our allies.

Are you suggesting we should put further impediments in the way of these people keeping up with their spare parts?

Ms. McCABE. No, that was not the suggestion.

Senator STEVENS. Well, the implication is here. My Subcommittee handles the Defense side of this and I think we know a lot about the relationships we have with these countries in terms of defense.

Ms. McCABE. No, we are certainly not indicating that.

Senator STEVENS. I certainly hope that you are not suggesting that we need more bureaucracy, more procedures for the Israelis to get parts for an F-15. Are you suggesting that?

Ms. McCABE. No, we are not suggesting that.

Senator STEVENS. And do you suggest that we need to have a criminal investigation of the people who are handling sales to the Israelis?

Ms. McCABE. We believe that information exists in Federal agencies—Justice, Commerce, DOD, Customs—that would be useful to the State Department when they are reviewing applications for commercial shipments. They should be aware of what information exists. They still will have to make a decision whether to issue the license or not.

Senator STEVENS. I would feel much more comfortable if you were suggesting to us that we ought to be sure that someone has been convicted of a crime, and says he is going to send something to Israel, actually sends it to Israel.

Ms. McCABE. Well, that is the concern, yes. And that is why the end-use checks would——

Senator STEVENS. That might be a concern. But to say he should be investigated when he makes the application is entirely a different matter, is it not?

Ms. McCABE. The end-use check would be done at the time of application. In other words, the U.S. Embassy would try to determine whether the sale was a valid sale, that it was truly going, say, to the Government of Israel as opposed to being shipped someplace else.

Senator STEVENS. Well, suggest that the end-use check ought to be done by someone in Israel checking to make sure it got there.

Ms. McCABE. Well, that is the Embassy in Israel. That is what we are referring to as end-use checks also.

Senator STEVENS. Well, I do have a problem with the inference that somehow all of these munitions are leaving the United States and that somehow or other the volume is increasing. There is tension all over the world and so our military sales increase.

Mr. Chairman, I am sorry. I do have to go. You have not suggested that any of these people have actually mis-directed their sales, right?

Ms. MCCABE. That was not within the scope of our review and we have no information on that.

Senator STEVENS. So, the fact that these people had a criminal record had to do with whether or not they should be trusted in the first place, as far as you are concerned?

Ms. MCCABE. It would only be a flag. State might want to look more closely at a particular license. OMC has very scarce resources and a huge workload. OMC has got to direct its attention to those particular licenses warranting the most attention and scrutiny.

Senator STEVENS. Would an FBI check satisfy this as far as you are concerned? Should we recommend the State Department send these for a name check to the FBI?

Ms. MCCABE. In some cases. In some cases the information is already available. We are saying use available information. We are not saying institute new investigations, just use available information.

Senator STEVENS. Thank you very much, Mr. Chairman.

Senator PRYOR. I have got to respond to Senator Stevens, who is my very good friend and whom I have worked with for years on this Committee. I am sorry if I left this impression, but I think he has drawn the wrong inference on what this hearing is about. It is not about selling arms to Israel.

It is about companies that today have been indicted or plead guilty of selling arms to Libya, to North Korea, to Chile; that have been denied the opportunity by the Commerce Department to enter into the export market; about companies that have plead guilty to serious export crimes. This is what we are after. It is not about sales to Israel, and I hope that we do not leave that impression.

Senator STEVENS. Mr. Chairman, the 127 applications, what country were they sending arms to? Certainly they were not sending them to Libya?

Senator PRYOR. No. In this case they sent them to North Korea.

Senator STEVENS. No, no. The 127 or 124 applications, whatever it is, that is pending by the person who was so indicted? He is not convicted yet, by the way.

Senator PRYOR. Well, I believe the countries include Pakistan, Ireland, India, and Sri Lanka.

Senator STEVENS. They are not convicted yet, by the way.

Senator PRYOR. I know they are not convicted. But our point is at OMC they do not even have a red flag system that demonstrates that these people may be on some kind of a questionable list and that is the point of this hearing. There are no checks, there is no balance.

Senator STEVENS. Mr. Chairman, I am not critical—I have to go—of your comments. I am critical of the inferences coming from GAO that those sales are in some way wrong, the applications for those sales are in some way wrong.

Senator PRYOR. I hate for Senator Stevens to go, too. This hearing has livened up. Senator Sasser?

Senator SASSER. Well, thank you very much, Mr. Chairman.

Senator PRYOR. You got here at just the right time.

OPENING STATEMENT OF SENATOR SASSER

Senator SASSER. It sounds like I did and I am delighted to be here. I want to commend you for convening these hearings and carrying the lion's share of the load in conducting these hearings.

Mr. Chairman, I would like unanimous consent to have included in the record at this point an opening statement.

Senator PRYOR. Without objection.

[The statement of Senator Sasser follows:]

PREPARED STATEMENT OF SENATOR SASSER

Mr. Chairman, I'd like to thank you and Senator Pryor for holding this follow up hearing on the important issue of Federal licensing procedures for arms exports. The February hearing produced some interesting information about the complicated process of military arms and services exporting, and I look forward to discussing GAO's findings with regard to the procedures and its recommendations on how these procedures can be improved.

The United States Government takes seriously its duty to regulate the commercial sale or military arms and services and to insure that these sales are consistent with U.S. foreign policy and national security interests. Even with the budgetary constraints which we are feeling all across the country, I believe it must be possible to improve coordination of efforts, to utilize existing information sources more effectively, and to take additional measures to insure that U.S. arms—some of the most sophisticated and lethal weapons in the world—to not wind up in the hands of those who would use them against us and our interests.

Senator SASSER. I just have one question. Ms. McCabe, the OMC on authority from the State Department can revoke licensing privileges. They can deny license requests because of prior export violations, and they can impose fines.

Now, according to your report—that is, the General Accounting Office report—the State Department has exercised this authority only four times since 1976 and the last time was in 1983. I bet that had something to do with Libya, just guessing.

But I am a little curious about the circumstances surrounding these four occurrences. What countries or persons were involved, that lost their license? How were the violations discovered? What measures were taken? Does OMC have detailed files on these case? Do you have any information on that?

Ms. MCCABE. Senator, we can get that information. We do not have it with us right now. We could get that for you.

Senator SASSER. Do we have anybody from OMC at the witness table?

Ms. MCCABE. Not at the witness table, no.

Senator SASSER. These are all General Accounting Office people?

Ms. MCCABE. Yes.

Senator SASSER. Well, perhaps OMC then could shed some light on that when it comes their time to testify. Also, we would like to get the reaction, for the record, of the General Accounting Office relative to this question.

[Information subsequently submitted follows:]

OMC AUTHORITY TO IMPOSE PENALTIES

The State Department has authority to revoke licensing privileges, deny license requests based on prior export violations, and impose civil penalties. It has used this authority four times since 1976, the last time in November 1983. Of the four instances, one resulted in a debarment (60 days); the other three resulted in fines of $7,000, $10,000, and $120,000. Two of the exporters were penalized because items exported were diverted to a proscribed country. Information on the other two export-

ers was not readily available. OMC may be able to provide more detailed information.

Senator SASSER. Now, the Office of Munitions Control [OMC], the compliance division—I think you may have testified before I got here—has three staff members performing compliance work: a director and two paralegals. You have indicated that they assist the U.S. Customs Service and the Department of Justice to ensure that arms exports are properly licensed and that violations are investigated and prosecuted, is that correct?

Ms. MCCABE. That is correct.

Senator SASSER. Has the size of that force changed over the past 10 years?

Mr. HOLMAN. Senator, I believe they added one staff member in the past few years, but it has been relatively stable over time.

Senator SASSER. They now have three people and we indicated that was a director and two paralegals.

Mr. HOLMAN. Yes, sir.

Senator SASSER. Looking at the chart over there with a 10-year growth of the case load at OMC, that appears to have gone up approximately 100 percent in the past decade. In that period of time they have added perhaps one additional staff person?

Ms. MCCABE. OMC does not view itself as an enforcement agency. They assist the enforcers—principally, Customs, and Justice. They assist them by documenting past exports and exporters under investigation by Customs or Justice. OMC is not initiating their own cases as much as they are responding to requests from the other Departments.

Secondly the compliance group does end-use checks. If our suggestion was adopted and there were more end-use checks, the compliance group would coordinate those. Then they may need additional people. We would not have any information on that right now because we do not know what the increased workload would be since guidelines have not yet been developed.

On the other hand, if they automated their computer system and they were able to quickly retrieve information rather than making manual searches through boxes of records, you might be able to cut the staff.

Senator SASSER. All right. Thank you very much.

Senator PRYOR. Ms. McCabe, this is sort of a theoretical question, and we are about in a very few moments to go to our State Department witnesses. Let's say the Soviet Embassy, or another Embassy in town, decided to go out and buy a weapon or munitions or a computer system of some nature, bought it from the black market, or went over into Arlington and bought it; took it back to the Embassy, put it in a Diplomatic Pouch and sent it to their home country. In such a case would the Diplomatic Pouch be immune from search? Is it protected? Do you know?

Ms. MCCABE. No, I don't.

Senator PRYOR. Mr. Huntington?

Mr. HUNTINGTON. We discussed this question yesterday a little bit and I talked to our Office of General Counsel. A specific provision was added to the Export Administration Act in 1985 that allows Commerce to control items being sent to Embassies. Our

lawyers were not able to find a similar provision in the Arms Export Control Act.

It might be a good suggestion to amend the Arms Export Control Act, but it is in the Export Administration Act as of 1985. You can control items going to Embassies.

Senator PRYOR. You can or cannot?

Mr. HUNTINGTON. Can.

Senator PRYOR. Are they controlled?

Mr. HUNTINGTON. We did not look at it. That is the Commerce Department. We only examined OMC. The Export Administration Act applies the Department of Commerce.

Under the Arms Export Control Act, we did not see any similar provision in the Act. That does not mean it is not there or it was not intended when the Export Administration Act was amended. But on short notice we did not do a complete search to determine what the intent of Congress was.

Senator PRYOR. During the investigation, was this ever alluded to? Was this a concern that you found expressed out there in the community?

Ms. MCCABE. Do you mean that foreign Governments could be purchasing military items that are on the munitions list and exporting them to their home countries via the Diplomatic Pouches?

Senator PRYOR. Yes. Was that concern expressed?

Ms. MCCABE. It is an interesting question but we have no information on that.

Senator PRYOR. Maybe we should not give them that idea, but I imagine that idea has been around for a long time.

It may well be that we may call some of you back to the witness stand. We are going to hear from Ambassador Holmes in one moment, but I wonder if there are any additions or comments that any of you would like to make at this time.

Ms. MCCABE. No. Thank you.

Senator PRYOR. Once again, I applaud you for this fine GAO report. It is going to serve, I think, a very constructive use, and I hope that you will stay around for the response from our State Department.

Ms. MCCABE. We will. Thank you very much.

Senator PRYOR. Thank you.

Our next witness this morning is Ambassador H. Allen Holmes, the Assistant Secretary for Politico-Military Affairs in the Department of State. Ambassador Holmes' bureau has direct oversight over the Office of Munitions Control. He is accompanied by Mr. Michael Matheson and Mr. Philip Hughes.

Ambassador Holmes, we welcome you to the Committee this morning. We thank you for appearing here to discuss the GAO findings about the OMC and the improvements that you may have initiated at OMC. We will try to keep the oral part of your statement, Ambassador, close to 10 minutes, and we also have asked the GAO personnel to remain throughout your statement if possible, if time permits, because there may be a time for response after this series of statements and questions.

TESTIMONY OF H. ALLEN HOLMES, ASSISTANT SECRETARY FOR POLITICO-MILITARY AFFAIRS, U.S. DEPARTMENT OF STATE, ACCOMPANIED BY MICHAEL MATHESON, DEPUTY LEGAL ADVISOR, AND PHILIP HUGHES, DEPUTY ASSISTANT SECRETARY FOR TECHNICAL AFFAIRS

Mr. HOLMES. Mr. Chairman, I appreciate the opportunity to appear before you and your colleagues to address the Government's munitions control function. Your hearing last February with the Director of the Office of Munitions Control looked into some aspects of the Office's operations and U.S. munitions licensing procedures. The GAO report we have just seen addresses other concerns somewhat different from the focus of your February hearing. I am happy to have this opportunity to contribute to your review of this function which is important to attaining our foreign policy objectives.

Today I would like to provide some important background on U.S. munitions licensing practices and to put the issues and concerns discussed so far into a broader policy perspective. I will be happy to discuss the points raised by the GAO's report. Regrettably, however, we did not receive the report in time to address it in detail in my prepared remarks.

The first point I want to make is the munitions control function is, first and foremost, a key foreign policy function. For half a century Congress has statutorily required regulation of private, commercial arms exports to ensure that these activities are consonant with, and do not conflict with or undermine, our foreign policy and security objectives. From the enactment of a joint resolution in 1935 and the Neutrality Acts of 1937 and 1939—to which we trace our modern legal authority to regulate U.S. commercial arms exports—through the Mutual Security Acts of 1951 and 1954 to the Arms Export Control Act of 1976 there has been a central guiding purpose for empowering the Executive Branch to regulate U.S. commercial arms exports.

That purpose has been to ensure that private arms traders, in pursuit of profit, do not ship arms to our enemies in war; do not arm hostile countries with whom we may have to do battle; do not ship arms in contravention of U.S. neutrality or to the military opponents of Allies or friends whose security is linked to our own; and do not ship arms in violation of legal arms embargoes or foreign policy restrictions on arms exports to particular countries.

Put differently, the central purpose of the munitions control function is to ensure that only commercial arms exports that contribute to or are consonant with our foreign policy interests are official authorized. Any unauthorized arms exports are, under the law, therefore illegal.

Our substantive foreign policy concerns affecting commercial arms shipments obviously have shifted over time. In the 1930s, our primary concern was preservation of our formal neutrality. We now have a variety of policy objectives that require effective regulation of arms exports:

One, enforcing international or unilaterally imposed legal arms embargoes;

Two, prohibiting arms exports to countries supporting terrorism;

Three, restricting arms sales to countries potentially hostile to the United States;

Four, restricting certain arms exports to repressive regimes where we have human rights concerns; and

Five, ensuring the adequate and timely supply of defense articles to our trusted Allies.

In addition, we have for foreign policy reasons restricted the sophistication of armaments we are prepared to exports to particular countries or even whole regions. Our considerations here are varied. We may seek to preserve regional arms balances at the lowest possible levels of technology and cost; at times we are concerned not to supply military capabilities excessive to any plausible regional threat; at other times we are concerned not to overburden the resources of the purchasing country.

In recent years we have become more sensitive to the technology transfer dimension of commercial arms exports. In particular, we do not want to erode our edge in key military technologies by their export, particularly in the form of technical data, to countries eager to copy or exploit these technologies for their own commercial gain or military programs.

Because the technical advice of the Defense Department has always been a key factor in determining what proposed arms exports are consonant with our foreign policy goals, it has been natural for the Defense Department to factor this technology transfer concern into its advice on sensitive or precedent setting arms export cases.

My point in emphasizing the essentially foreign policy nature of the munitions control process is this: so long as we manage this process as first and foremost a foreign policy matter it is relatively easy to factor into the approval process the range of other concerns—military balances, technology transfer, et cetera—that impinge on those decisions. Were we to manage this process as other than in the first instance, a foreign policy matter, it is difficult to see how our overarching foreign policy interests could be adequately factored into our munitions control decisions.

A second point I would like to make concerns the nature of export licensing systems and what it is reasonable to expect them to do. As you know, a large number of countries operate export licensing systems for munitions items and dual use products. The 16 members of COCOM, as well as some cooperating countries, maintain export licensing systems for dual use strategic exports. Some other countries maintain export licensing systems for short supply, currency control, or foreign policy purposes. And every country that we know of that engages in munitions transfer has some system of officially licensing or approving these transactions.

Our export licensing system—particularly for munitions items—achieves the same two effects that such systems do in other countries: First, it informs the shipper what he is authorized to export and under what conditions, and what he is not authorized; and second, it identifies for Customs and other enforcement authorities, both at the port of embarkation and along the route to the final destination, those shipments that have been authorized and the destinations for which they are authorized.

It is very rare in COCOM countries that major technology diversions to the Soviet bloc are discovered in the process of issuing an export license. This is not because of laxity. The fact is that such technology diverters rarely apply for approval to ship strategic goods to forbidden destinations, or apply for licenses in such a way as to tip off authorities to the diversion they plan as the goods are in transit. Rather, they seek to sidestep the licensing process entirely or deceive either the licensing authorities or customs authorities or both.

Similarly, it would be rare, to say the least, for anyone seeking, for example, to smuggle arms to the Irish Republican Army to register with OMC as an arms exporter and apply for a license to do so. They know that any application for such a license would not be granted. It would be equally unexpected for anyone seeking to defy our arms export bans to Libya or Iran to apply for an OMC license to do so. They, too, know what the answer would be.

Incidentally, I might insert here just as a comment that not too long ago when we were reviewing our files at the time of the Iran/Contra hearings I found quite a number of license applications for pieces of equipment to Iran which were dismissed, which were rejected.

It would be very helpful if such potential diverters, such people, would advertise imminent violations of our law in this way. Unfortunately, they usually do not.

These examples highlight what an export licensing system can and cannot do. It can ensure that only shipments in consonance with law and policy receive official approval. It can, with proper examination of applications, scrutinize proposed exports to ensure that there are no prima facie grounds to believe that the export will end up in some place or be used for some purpose not intended. Licenses notify Customs and other enforcement authorities of which shipments have been properly authorized for what destinations. Absence of a license, or appearances of fraud or irregularity in licenses, provide grounds for suspicion and further enforcement inquiries and action.

No licensing system alone can ensure that no one will ever attempt, or even succeed, in exporting without a license. No licensing system alone can ensure that properly authenticated and approved exports will not be deliberately misdirected once they leave the country. And no licensing system is proof against deliberate and perhaps sophisticated deception, although prudent checks can reduce this risk somewhat. These are the areas where the support of enforcement agencies come in. Without their contribution there are severe limits on the ability of an export licensing system alone to uncover prospective or in-progress violations.

I make these points only to say that, first, we must measure the effectiveness of our munitions licensing operations against realistic standards and expectations; and second, we must not evaluate OMC's operation as if it were solely responsible for all facets of the munitions control system—a system that involves contributions by several Departments and Agencies.

Against this backdrop, I think we should bear in mind what OMC is doing in support of our foreign policy and security interests in regulating commercial arms sales abroad. We currently have

complete arms embargoes in force against 28 countries—including, for example, the nations of the Soviet bloc, Libya, Iran, and South Africa. OMC has not licensed any weapons exports for these countries.

We currently have restrictions on sales of certain types of arms to seven countries because of human rights concerns and other restrictions on certain munitions licensable articles to seven countries because of nuclear non-proliferation concerns. To the best of our ability to determine, OMC has licensed none of the restricted items to the countries in question without explicit exceptions approved by higher authorities.

We have policy restrictions on the level of sophistication of military hardware that can be sold to particular countries—for example, China, India, and Taiwan. To the best of our ability to determine, OMC has issued no licenses outside the bounds of these restrictions without either full interagency concurrence or the authorization of higher level authorities.

We have in place policies which forbid the export of some unique and highly sophisticated munitions items, and other policies which make only particularly close Allies eligible for exports of other sensitive defense items. To the best of our ability to determine, OMC has not licensed the export of any items that as a matter of policy are not to be exported and has not licensed any exports of restricted munitions items and technologies to countries other than those eligible to receive them. And of course, to the best of our ability to determine, OMC has not authorized any exports of U.S. arms by or to known terrorists, gangsters, or assassins.

I make these points—which might seem obvious—only to ensure that we do not lose sight of one key fact: our munitions control system is apparently serving effectively the main foreign policy and security objectives that we have set for it.

It is true that the workload of munitions licensing has expanded greatly in recent years. In part, this reflects a shift from government-to-government arms transfer to commercial sales as FMS funding has declined in recent years. Many friendly nations are making more commercial purchases to maintain equipment we have previously supplied to them to sustain their armed forces. In part, this increase also reflects the development of important treaty relationships with key allies with whom we maintain critical common defense arrangements and to whom we export a great deal of defense equipment.

The 100-percent increase in OMC's volume of license applications over the last 10 years, with no increase in staff, has admittedly strained OMC's resources and we have come to recognize in the last year and a half the limitations of OMC's hard-copy file storage capacity and of its automated records pose severe impediments to carrying out the kind of routine checks on license application data that should be readily available in our modern world of automation.

Finally, OMC's chronic shortage of clerical personnel has slowed much more than we would like the process of final license issuance once interagency comments are recommendations are received.

That is why we welcome your Committee's inquiry into this field. It has reinforced our own diagnosis of needed improvement in

OMC's operations, has given impetus to some initiatives that were already in progress, and has stimulated some new ones. Let me briefly review some of they key steps that we have been taking to upgrade OMC's capabilities.

As I believe you are aware, we have approved a productivity improvement plan developed last year for OMC which contemplates both a 50 percent staff increase as well as significant internal reorganization and some hardware procurements. This plan is intended to streamline OMC's internal processes to eliminate current bottlenecks and speed up the mechanical parts of licenses issuance. But equally important, it is intended to improve the quality and thoroughness of licensing review, both by making more people available to support such reviews and to request end-use checks from Embassies abroad, and by putting on-line automated records at their disposal to make possible increased efficient screening of applications and systematic checking of precedent cases.

This plan explicitly contemplates creation of a compliance division, one of the major functions of which will be to keep track of exporters' compliance with registration and reporting requirements as well as providing enhanced support to enforcement activities and prosecutions. Since the adoption of this plan, the Department has selected OMC to participate in the President's Productivity Program. As a result, OMC has committed to make specific improvements in the timeliness of its routine license issuance and final license issuance after the interagency reviews are complete.

We have had rather good success with all the procurements contemplated in this plan, acquiring essentially all the equipment contemplated in the plan during the last fiscal year and in this one. Quite frankly, though, in the budget and personnel environment the Department now faces, we have been less successful in securing the personnel called for in our plans.

We have recently taken steps to implement the key recommendations of the Management Survey Team that we earlier asked to study OMC's operations—the institution of "public hours" to receive outside inquiries about license status, in order to free more uninterrupted time for review of license applications, and a reorganization of the way licenses will be processed within OMC. These steps, also, will contribute both to the efficiency and thoroughness of license reviews.

We have, since your February hearing, issued a procedures manual to OMC officers to collect in one place the written guidance under which they have been operating to guide their handling of munitions license processing. We have also taken steps to ensure that OMC has always on hand the complete list of "denied parties"—persons or organizations debarred by other Departments from export activities—to be able to take into account OMC's license review.

It remains our belief, however, that we lack legal authority to debar an individual from export privileges under the ITAR solely because of his violation of other acts. We may base a debarment upon the issuance of a Department of Commerce denial order under certain circumstances. However, we are not even empowered to debar a person for violating the Arms Export Control Act absent

conclusive proof of the violations established as a result of a criminal conviction or a separate administrative due process procedure.

In February we proposed legislation to authorize, in addition to normal appropriations, use of up to $100,000 annually of OMC's registration fees to expedite the final issuance of munitions licenses. Both the House Foreign Affairs and the Senate Foreign Relations Committees have included this provision in their respective Foreign Assistance bills; the House Committee even increased the amount to $250,000. We would welcome your support in seeing that this provision is included in the final fiscal year 1988 legislation.

Finally, we have recently received a major funding allocation by the Department for $500,000 for a partial overhaul of OMC's automation capabilities. We recognize that additional resources will be necessary to complete the job. Now, with the resources in prospect to achieve the kind of modern automation capability OMC needs for record storage and retrieval to support licensing reviews and for modern word processing to support license issuance, we have embarked on an automation systems requirement study to ensure that we use this unique opportunity to procure a system that truly meets OMC's needs. Only after satisfactory completion and review of this study will we proceed to procurement.

I hope that my remarks have underscored that the State Department regards the effective regulation of U.S. commercial arms exports as important to our foreign policy and security interests. U.S. industry is a partner with the U.S. Government in maintaining a strong United States defense posture. It is the Government's responsibility, however, to ensure that overseas arms exports support our foreign policy goals, including meeting the legitimate defense requirements of trusted Allies.

We have always taken, and always will take, this responsibility very seriously. Against the background of what is reasonable to expect our export licensing procedures to accomplish, we believe that the Government's munitions control system is fulfilling quite well the key policy tasks set for it. Of course, there is always room for improvement and we intend to make those improvements.

We have recognized, as you have, some areas where both greater efficiency and more thoroughness is warranted. We believe that we are taking reasonable, appropriate and expeditious steps to strengthen OMC's operations in these areas. We appreciate very much your interest in this area and your support for our efforts to strengthen OMC.

Thank you, Mr. Chairman.

Senator PRYOR. Mr. Ambassador, how long have you occupied this present position in the State Department?

Mr. HOLMES. Two years, Mr. Chairman.

Senator PRYOR. Now, I am assuming you have personally visited OMC?

Mr. HOLMES. I have, Mr. Chairman, but not as often as I would like.

Senator PRYOR. When was your last visit?

Mr. HOLMES. My last visit was about a year and a half ago. I should add, however, that I meet with the Director of OMC or his deputy on at least a weekly basis.

Senator PRYOR. So, I assume, Mr. Ambassador, that you have seen the application form, DSP-5?

Mr. HOLMES. Yes, I have.

Senator PRYOR. Does it concern you that you do not even have to be a citizen to become an arms exporter?

Mr. HOLMES. Well, it does not concern me when you consider for example that the Israeli Defense Procurement Office in New York is a customer.

Senator PRYOR. Well, you know, I do not know why this hearing has evolved itself into a question of Israel.

Mr. HOLMES. Or, for that matter——

Senator PRYOR. My very good friend, Senator Stevens, thought that that is what this was about. That is not what this hearing is about.

Mr. HOLMES. I cite it only as an example. There are other Allies that have procurement operations in the United States and the vast majority of our exports of munitions items—I would say probably 70 to 80 percent—are equipment that go to Allies, based on long-standing relationships and to give them spare parts and munitions as part of a common defense effort. So it really does not trouble me that other than U.S. citizens can apply to license exports.

Senator PRYOR. All right. Does it trouble you that down in the office—I have some pictures, by the way, of that office. I think these are pictures of OMC. There they are. They look like very nice people operating sort of a paper mill down there over in Rosslyn. I want to talk about that in a minute.

But does it concern you that on this application form the applicant does not have to state whether or not he has been a felon or guilty of treason or guilty of violating the Trading With the Enemy Act? Does that concern you in any way?

Mr. HOLMES. Of course, any applicant could always lie, mis-represent, could lie in answering such a question. But I personally would have, obviously, no objection to including that kind of a question on the form.

By the way, let me correct, if I may, Mr. Chairman, one statement that I earlier made. It has just been brought to my attention. To register, one must be a U.S. citizen or a permanent resident. Non-permanent resident foreigners cannot register, except for foreign embassies. Embassies can.

Senator PRYOR. Well, on this license application there is no reference to whether or not that person or individual is a citizen of this country or not. Mr. Hughes?

Mr. HUGHES. But Senator, when the license application is submitted, the first thing that is done is that the application is checked against the list of registrants to determine if the party is registered or not. If you cannot be registered unless you are a U.S. citizen or a permanent resident alien, or a foreign embassy in the United States or a similar operation like the Israeli Procurement Mission or the Federal Republic of Germany's procurement operation, in effect, a shipping operation at Dulles Airport—if you cannot be registered except under those conditions and the license application comes in and it is for someone who is not a registered party, then it is not approved. And if they are a registered party,

then they are either a U.S. citizen, a permanent resident alien, or a foreign embassy.

So it seems to me that through the registration process the fact of citizenship is established independent of whether the question is asked on the form.

Senator PRYOR. I am trying to find out some internal workings here of OMC, if I might. I was not thinking of asking this question until you raised it. Where does the West German operation work from? I did not know of that——

Mr. HUGHES. There is a facility at Dulles Airport that the German Government routinely sends aircraft to. They bring equipment here for repair. They send equipment out.

Senator PRYOR. Is it a procurement office, basically?

Mr. HUGHES. My recollection is it is more like a shipment office.

Mr. HOLMES. It is an aviation facility, basically.

Senator PRYOR. Are there other procurement offices that other countries operate in this country that buy hardware and weapons from the United States? And if so, what countries have those and where are they?

Mr. HUGHES. There are. We will have to get you a list of them.

Mr. HOLMES. The United Kingdom has one. But I will be happy to supply the whole listing for the Committee.

Senator PRYOR. I just think that would be interesting to get the flavor of what we are talking about here.

[The information referred to follows:]

May foreign governments have purchasing/procurement missions and offices in the U.S. Some are part of their embassies while others are completely separate. The most active of these missions and offices represent the Governments of the United Kingdom, Federal Republic of Germany, France, Turkey, the Netherlands, Portugal, Belgium, Greece, Sweden, Italy, Canada, Israel, Egypt, Brazil, Argentina, Australia and New Zealand. Licenses frequently are issued to these and other embassies, and directly to the UK, Netherlands, Egyptian and FRG procurement offices. Many embassies employ U.S. purchasing agents and freight forwarders to obtain their licenses.

The Taiwanese also have an active procurement mission in the United States.

Senator PRYOR. Now, Mr. Ambassador, if you would kindly look at that chart, those companies that either plead guilty or are pending trial, and violations of various acts, Trading with the Enemy, et cetera. Does it concern you that they are still being granted licenses by OMC?

Mr. HOLMES. Well, the short answer is yes and no. I say that because I think it is important and—I have to tell you, Mr. Chairman, I do not have in my head all the details of all of these cases and I would be very happy to supply detailed answers to the Committee on each one of these cases—but let me just say that as a general proposition, first of all, if, for example, a company is under a temporary denial order by the Department of Commerce—which I believe was the case with the Associated Industries case—that does not give us the authority to——

Senator PRYOR. Why?

Mr. HOLMES. We simply do not have the authority under the act or the ITAR to debar such a company on the basis of a temporary denial order. I am told that on the basis of a full denial order, yes. But not a temporary denial order. I am told that in this particular instance at a certain point the temporary denial order was lifted.

Now, a large company the subsidiary of which or an officer of which might commit a felony, the question is whether to debar a large corporation for the action of one subsidiary or one individual. I think in the interest of due process one would have to look at such a case very carefully. Now clearly, if one officer or one subsidiary of a company commits a crime, we fully support prosecution of this crime and the requisite punishment.

But, for example, under the AECA, Section 38 I think it is, the Congress did not give to the judicial/criminal process, it did not give them debarment as a criminal punishment. There are various fines. I think up to $1 million and 10 years in prison, if I am not mistaken, are some of the criminal punishments which can be meted out by a judge, and we fully support, obviously, this kind prosecution.

Debarment, however, even if it were available to a judge, is a procedure that should be used sparingly. After all, a company which, for example, provides important and legally constituted arms exports to trusted Allies, should not be penalized across the board, it seems to me, on the basis of fairness and our foreign policy interests, because one officer or one division of it may have been convicted of a felony which could be a serious one or could be a technical violation.

Senator PRYOR. Well, Mr. Ambassador, let me cite you, if I may, Section 126.7 of your own regulations in the State Department:

> An export license may be disapproved whenever the Department of State deems such action to be in the furtherance of world peace, national security, or the foreign policy of the United States.

Here we have several companies—in fact I have a much longer list of many of these companies that are in trouble—that continue to get licenses to export arms overseas. Now, you say you lack the authority. What about foreign policy? What about national security if a company or an individual has plead guilty or is even in the indictment stage for selling arms to North Korea or to Libya or to Chile or Pakistan or wherever?

I do not see your rationale whatsoever. I do not see how you can say you do not have this authority.

Mr. Hughes may want to respond to that. I am not trying to grill you. I am trying to say that you are making a very, very inconsistent and, I think, legally wrong—you are coming legally to the wrong conclusions. Mr. Hughes?

Mr. HUGHES. Senator, I think it is quite true that Section 126.7 does provide very broad grounds for denial of license applications. License applications are denied. You heard Ms. McCabe testify that about 6 percent are denied outright and a further percentage are denied in effect through "return without action" actions by the Office of Munitions Control.

But in the case of someone who has been indicted for an offense—let's say it is an export control related offense, an offense related to the Export Administration Act or the International Emergency Economic Powers Act, Trading with the Enemy Act, or specifically, the Arms Export Control Act. Indictment is not the same as conviction. After all, people are sometimes acquitted.

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Were we to take action, merely on the basis of accusation, to deny particular licenses or to debar particular companies, absent the conclusive proof of guilt, we could be, I think fairly, said to be penalizing companies, frankly, wrongfully. The fact of indictment definitely should be and must be a factor in the scrutiny of export licenses. If an applicant is applying for an export license and he is under indictment, we must, should, and now do look very carefully at that export license to be sure.

Senator PRYOR. How do you know that a company principal in a company is under indictment?

Mr. HUGHES. We now have in——

Senator PRYOR. Since when?

Mr. HUGHES. We now have since the last month in the Office of Munitions Control up-to-date—and we will have for the future—up-to-date lists of the Commerce "denied parties" list and the Justice Department list of significant export cases or export prosecutions in progress, which will be systematically screened by the license officers. In fact, all the license applications will be pre-screened before they ever go to licensing officers to determine whether any parties to the transactions appear on those watch lists.

Those procedures have been implemented. I think the Ambassador would agree with me in saying that this is a direct result of this inquiry of the GAO that you have kicked off that has pointed up this need. It has been a very valuable contribution. The procedures have been implemented. When, as Ambassador Holmes' statement says, we get around to being able to actually install what we could call a thoroughly modern automated capability, that screening will occur in an automated fashion using a database for a screen, not just manual lists, and it will happen. It does happen now.

Senator PRYOR. Let me ask you this. Mr. Hughes and Mr. Ambassador, I hate to call it this, but at the moment I can think of no better terminology. Are you going to have and keep a "bad guys" list—those people who are in trouble, who have been indicted, who are suspect, who have plead guilty? We are not talking about just indictments here. We are talking about pleas of guilty in many of these cases.

Mr. HOLMES. True. Yes, in fact, in other words through the provision of these lists, having access to these lists, files will be flagged as a result of this. As a matter of fact, I believe I am safe in saying that we have checked the current list of registrants against the Department of Justice and Commerce's lists that Mr. Hughes just referred to and there are no registrants that are on those lists.

But we will keep those lists and we will update them and have them available to scrutinize when license applications are received.

Senator PRYOR. Do you have that authority? Can you do this?

Mr. HOLMES. Yes, we have that authority. Do you mean the authority to use these "denied parties" lists?

Senator PRYOR. And can you keep these lists? I think there may have been a statement in the GAO report that was giving the position of OMC that because of the Privacy Act or the Freedom of Information Act you could not keep these lists. Is that not your position?

Mr. HOLMES. I would like to ask Mr. Matheson to respond to that, Mr. Chairman.

Mr. MATHESON. Yes. It is not a question of our ability to keep the lists, but there had been some concern in the past that if we kept such a list there might be requests under the FOIA or the Privacy Act for its disclosure. We are looking now at those questions in the Legal Advisors Office, but there have been some changes in the relevant provisions of the FOIA, particularly the law enforcement section, which I think as a preliminary matter will enable us to handle that problem.

The Privacy Act question is a little bit more complicated because the law enforcement provision is somewhat different. But I think it would be safe for me to say that I believe we can handle the problems.

Mr. HUGHES. I might add, Senator, that the list that I was making mention of and I think that Mr. Matheson has been making mention of are lists that are, after all, compiled by other agencies who have enforcement or licensing responsibilities. Those are not lists generated in the State Department. Part of the concern that you saw reflected in the remarks reported in the GAO report from OMC staff members was a concern about lists that might be generated from within the State Department itself, a sort of State Department generated "bad guys" list. That is, I think, a somewhat different matter from the lists that are compiled by other agencies.

Senator PRYOR. Well, let me first just say that I think it is an absurd argument to say that you do not have authority, or to hide behind the Privacy Act and saying you cannot keep lists. In fact, the State Department Privacy Act regulations specifically exempts munitions control records, which I would assume would be OMC. I think you are specifically excluded from the Privacy Act and from the Freedom of Information Act.

Mr. HUGHES. Senator, if I might clarify on that point, that exemption applies to munitions control licensing records; that is the proprietary information—at least it is my understanding—that it applies to munitions control licensing records, the proprietary information which is potentially either beneficial or harmful to the firm involved or to competitive firms.

As Mr. Matheson said, we are still exploring the Privacy Act implications of having certain private persons appearing on such lists. We are not saying that we cannot keep lists. We are saying we are in fact using other agencies' compiled lists precisely as the GAO recommended. We are simply saying that we are exploring a particular legal aspect of this issue.

Mr. MATHESON. What I think we need to be able to do, Senator, is to be sure that we can use the broad law enforcement exemption in the Privacy Act for this general category of information. As I say, we are looking closely at it. I have a feeling we can solve this problem.

Senator PRYOR. You have a feeling what, Mr. Matheson?

Mr. MATHESON. That we can solve this problem.

Senator PRYOR. Well, I will tell you what. You have a big problem to solve because I think that in order for the State Department to keep OMC, you are going to have to make some very drastic

changes—very drastic changes. Now you say, well, we have just started keeping better records. That is one change. But we are going to have to really see a lot of major changes, I think, because OMC is a highly sensitive agency.

Frankly, I hate to say this because I know that some of the OMC people are here, but I think it is an agency that no one wants. I do not believe the State Department wants this agency.

Mr. HOLMES. We want it.

Senator PRYOR. I do not think that the Department of Defense even wants this agency; maybe they do. For awhile I thought maybe Customs wanted it. I do not think the Customs Department wants the agency, or the Treasury Department wants the agency.

This is a very strategic agency of our Government that functions with 30 people including three enforcement individuals, and they are setting major international policy about who gets export licenses to sell arms. You are not even tied in with the Commerce Department computer system or the Department of Defense computer system. And to come here and tell us what the purpose of munitions control should be does not jive with what OMC is actually doing.

In fact, Mr. Ambassador—and you respond to me and you rebut this if you think it is a unfair accusation—about a third of your statement this morning you talked about increasing productivity. In other words, processing more licenses. Not checking, not qualitative, not background checks, not getting to the end-use countries to see where in the world these arms are going. You are talking about productivity and processing papers and licenses so it will be more convenient for the arms exporters.

That is where I see you coming from here rather than trying to tighten up who we grant licenses to.

Mr. HOLMES. No. Mr. Chairman, I do have to disagree with that interpretation.

Senator PRYOR. You are free to disagree.

Mr. HOLMES. The President's Productivity Program—and we are trying to apply it to OMC—includes improving the quality and the thoroughness—and I believe my statement says something along that line—of this operation. So it is not accurate to say that we are simply interested in productivity from the point of view of increasing the rapidity and number, being able to handle a larger number.

I would like to respond to an earlier point you made. I think it is very important that this be in the record. The Secretary of State, the Department of State, does want the Office of Munitions Control under its jurisdiction. We think it is a very important process, and so does the Administration.

The Administration's position is that the President has delegated the munitions control function to the Secretary of State because it is first and foremost a foreign policy function. Moreover, the Administration does not favor legislation that would remove the President's authority to delegate functions as he deems appropriate. Virtually all authorities in the Arms Export Control Act are given to the President and this should not be an exception.

I would just like to say that for the record, Mr. Chairman.

Senator PRYOR. How many more people are you going to ask for in the enforcement division of OMC? By the way, IRS is asking for

8,000 new IRS employees this year. How many are you asking for in enforcement.

Mr. HOLMES. First of all, Mr. Chairman, we do not consider ourselves an enforcement agency. However, as a result of some of the problems that we have encountered and the recommendations brought out by earlier studies we have done and the GAO report, we are creating a compliance division and we will increase our resources in that from—I think there are three now—to eight, including a full time attorney.

That is our plan. We do not have those resources yet but we have requested them. As a matter of fact, our total resource request in people is 15, which would be a 50 percent increase of our present complement and we are asking I think about two-thirds of that—I think it is 10—are in our fiscal year 1989 request.

Senator PRYOR. You are still going to be processing, and I assume that it is going to grow from 50,000 upward each year. You are still going to have about 45 total people. I do not know how they process all of those. Physically, I do not know how you do it. Even if you did not read anything, just stamping them in and out, I think would be full time.

Mr. HOLMES. Well, they work hard and long hours. What they have done is to devote additional resources from the management cadres at OMC. Originally we had five licensing officers. Now the Director and the Deputy Director, his Special Assistant and the Chief and the Deputy Chief of the Licensing Division, those five individuals in addition help with this process. That is not an ideal situation. It is a way of meeting the demands, but I am looking forward to the day when we have those additional resources in hand so that we can put this on a more methodical basis and allow those officers to carry out fully their managerial responsibilities.

But we are trying to make do. We are using now, as I said, the lists available from other Departments. We are getting cooperation from the Department of Defense when we refer cases to them for advice.

I think the other thing I should point out is that through years of working on this they have developed a familiarity with these cases and the vast majority of these cases require only about 5 days processing because they are known exporters to known destinations, mostly in Allied countries which involve the supply of spare parts and ammunition and other equipment for defense purposes that are well known to us.

Senator PRYOR. Mr. Ambassador, the end-use issue of where these materials, commodities, weapons, and munitions wind up—spare parts, whatever—is an issue, I think, that really concerns this Committee. Now, you say that you are going to beef up that inspection program on end use. Tell us how you are going to do this. Detail that just a moment for us.

Mr. HOLMES. Yes. We agree completely with that recommendation that the GAO report made and we do intend to ask for more end-use checks. It will require additional resources. It may sound simple, but the process of putting down into a cable detailed information for use by an Embassy in checking on end-use takes time; it takes clerical time. We are already doing this to some degree. We want to be able to do it more.

I would like to add one other consideration here. You know, there are certain countries that are not too happy about what they conceive to be the sort of extraterritorial reach of the United States. I mean, we do have to move carefully and within the laws of the host country in checking on end use. I just would like to flag that as a consideration as we move to expand our end-use checks.

Senator PRYOR. You say you agree with the GAO report regarding the end use, let's say, laxity or whatever reason that it is not being done appropriately.

Mr. HOLMES. I agree with the report that we should expand end-use checks.

Senator PRYOR. And then I asked you, what are your plans to expand, and you say, well it is going to take additional clerical, and then it got pretty fuzzy.

Mr. HOLMES. It is part of our plan in our productivity upgrade and in the creation of this compliance division it is our intent to expand end-use checks through our Embassies.

Senator PRYOR. Are you going to additionally screen the applicants for these export licenses for their end-use, about the end-use of these products?

Mr. HOLMES. Well, we screen the applications now. If, for example, there is a suspicion of a possible diversion based on information that we receive from other agencies or, indeed, from our own files, obviously that leads to further scrutiny.

Senator PRYOR. You are going to tie-in then to the Customs computer and the DOD computer and the Commerce computer?

Mr. HOLMES. We do work with Customs. One of the things that we have in mind is to have—when we do have additional personnel—to have more hands-on visits, to have an officer from the Office of Munitions Control go from time to time to Customs and work with them. We do have to rely on them, however, for the return of licenses that have been used.

Senator PRYOR. Well, I will tell you what we are going to do right now. I do not know if this is appropriate or not, but I am just going to ask you and your colleagues to come back here 6 months from today, or we will just say 6 months, and give us a report on what has been implemented and what has not and we are going to utilize some oversight over OMC.

You say you agree with GAO on that section. Now, is there any part of the GAO report that you or your colleagues do not agree with? Is there anywhere you find disagreement with their findings?

Mr. HOLMES. Well, I would basically support their three main recommendations.

Senator PRYOR. Their what?

Mr. HOLMES. The three main recommendations that are in the report. The three recommendations are: Use readily available information on parties involved in arms exports to help identify export license applications requiring closer scrutiny. We certainly agree with that.

Develop procedures and criteria for requesting that U.S. Embassies help verify license application information. We agree with that.

Ensure export or compliance with administrative and reporting requirements. We certainly agree with that as well.

As I say, we are already implementing either fully or to some degree these recommendations. Further implementation will require additional resources.

We would like to thank the General Accounting Office for their help in giving higher profile to the requirements of our Office, and I would also like to ask for the support of your Committee for our additional resources.

Senator PRYOR. Mr. Ambassador, talking about support, would you support DOD and Customs support and their help in their assisting you in OMC to screen applicants for licenses?

Mr. HOLMES. Actually, they do that now. When we refer cases that are particularly sensitive or raise question marks with respect to the export of sensitive technology, for example, we do refer to the Department of Defense and we do get their cooperation. We need it and I believe we can count on their continued help in this matter.

Senator PRYOR. Mr. Hughes?

Mr. HUGHES. Well, perhaps I could further elaborate on what Ambassador Holmes said. We have, as you perhaps know, a permanent Customs liaison officer assigned to the Office of Munitions Control. There is a Customs computer terminal in the Office of Munitions Control to enable us to query back and forth when questions arise about suspicious shipments that Customs has found at ports.

We have asked the Defense Department to provide us a terminal that would connect to their computer system. This has been talked about. It has never actually been followed through. At least our Defense colleagues have not given us the terminal. But we are more than happy to make use of it.

We do, as Ambassador Holmes mentioned, refer those cases which are sensitive, precedent setting, or that otherwise require more than a sort of normal degree of scrutiny within the Office of Munitions Control, we refer those cases out and the bulk of those cases are referred to the Department of Defense and they do cooperate in providing advice, including from their intelligence database.

Senator PRYOR. Now, are you going to do the same with Commerce? Because DOD only does about 15 percent of the licenses that is in their area. Are you going to get a full cooperation with Commerce? Are you going to be tied into that system?

Mr. HUGHES. Senator, for the purposes of screening applicants—that is, to try to determine whether the parties to the transaction are suspicious parties or not—that is, frankly, the only aspect of the munitions licensing process—the actual issue of licenses—that could conceivably involve the Commerce Department. We are not required, either by statute or——

Senator PRYOR. Well, that is not a bad reason, though, is it?

Mr. HUGHES. No. I understand. But we are not required to refer individual license applications to the Commerce Department for their opinion about whether this or that item should be exported.

Senator PRYOR. Mr. Hughes, I know you are not required to. In fact, OMC seems to think is not required to do anything. I am saying, why do you not order OMC to aggressively go to the Commerce Department and get involved with that computer system so

that OMC will know for a fact who has been denied licenses to export commerical items overseas?

Mr. HUGHES. We are doing that. We are not doing it on-line.

Senator PRYOR. Pardon?

Mr. HUGHES. We are doing that. We are not yet doing it on-line.

Senator PRYOR. You are just beginning this, is that right?

Mr. HUGHES. It is being done with the lists, hard-copy lists.

Mr. HOLMES. One point of possible interest, Mr. Chairman, is, it is my understanding that whereas the Office of Munitions Control rejects about 6 percent of the license applications, that in the Department of Commerce it is about 1 percent.

Senator PRYOR. They reject about 1 percent?

Mr. HOLMES. That is what I am told.

Senator PRYOR. I have a table somewhere that shows that Commerce has 140 enforcement personnel where you have only one plus two paralegals at the present time. A total of three enforcement personnel. A total of three.

Mr. HUGHES. Actually, Senator, we have zero enforcement personnel.

Senator PRYOR. Zero.

Mr. HUGHES. We have compliance personnel. The Commerce Department is legally empowered to enforce. They go and make investigations. They can make arrests. They can even carry, I believe, firearms. Those are not powers that are given to the State Department at all, by law or regulation. At least, for this function.

Senator PRYOR. For the record, and I want the record to indicate this. We had a discussion a moment ago—we are about to conclude—we had a discussion a moment ago about the Freedom of Information Act and Privacy Act and the GAO finding that OMC has, "not formally developed a list of questionable firms"—I am quoting from page 13—"and individuals out of concern that such lists would be subject to public disclosure under the Freedom of Information Act, or disclosures to affected individuals under the Privacy Act."

I just wanted the record to indicate which page of the GAO report I was referring and I am very hopeful that OMC is going to keep a much better watch list and know that it is exempt from Privacy Act and Freedom of Information Act reporting requirements.

I just also will state at this time that we possibly will—and I think there may be one or two other Senators wanting to participate—submit questions in writing to our witnesses this morning.

I would also like to give the opportunity to any member of the GAO staff to respond to any statement or clarify any matter that has been brought before the Committee this morning. We welcome you to return to the witness table should you desire.

Mr. Ambassador, any final response?

Mr. HOLMES. Thank you. We will be very happy to respond to the subsequent questions when we receive them.

Senator PRYOR. Thank you for appearing and this meeting is adjourned.

[Whereupon, at 12:03 p.m., the Committee adjourned subject to the call of the Chair.]

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

United States General Accounting Office

GAO Testimony

The Office of Munitions Control Can Strengthen Its License Review Process

Statement of
Joan M. McCabe, Associate Director
National Security and International
Affairs Division

Before the
Committee on Governmental Affairs
United States Senate

GAO/T-NSIAD-87-41

78-628 0 - 88 - 4

Mr. Chairman, Members of the Subcommittee:

I am pleased to be here to discuss our report on the State Department's Office of Munitions Control (OMC) and its arms export licensing activities.[1] Our examination focused on OMC's license application review process and exporters' compliance with certain administrative and reporting requirements.

Our review disclosed a number of areas where OMC can improve its license application reviews to help ensure that proposed exports are legitimate transactions and conform with U.S. foreign policy and national interests. Although OMC processed most license applications in less than a month, we found that

-- OMC did not routinely check export license application data and information and rarely requested U.S. embassies' assistance in verifying the bona fides of the purchaser or other foreign parties to the sale.

-- OMC's facilities and automation capabilities are not sufficient to provide much assistance to licensing officers during their reviews,

-- OMC does not have adequate systems and procedures to ensure that exporters comply with administrative requirements, and

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[1]Arms Exports: Licensing Reviews for Exporting Military Items Can Be Improved (Sept. 9, 1987, GAO/NSIAD-87-211).

-- OMC understates the values on authorized arms exports and exports actually made in its reports.

OMC officials stated that an increased work load and static resources have restricted their application review efforts, including their ability to ensure compliance with all administrative requirements. OMC's volume of munitions cases (license applications and other requested approvals) has increased from about 26,000 in 1977 to over 49,000 in 1986 and is expected to exceed 52,000 in fiscal year 1987. Over the same period, OMC's staff has remained at around 30 persons with 10 staff members authorized to review licenses. OMC has prepared a plan to increase staffing levels and improve its automated systems, but important features of the plan are likely to be curtailed due to budget limitations.

BACKGROUND

The United States transfers military items and services overseas in two major ways: (1) U.S. government sales and grants under the Foreign Military Sales Program and the Military Assistance Program, respectively, and (2) commercial arms sales by individuals and business entities. For commercial arms sales, the exporter must have a U.S. government export license approved by OMC. OMC issues export licenses for items which are inherently military in nature, ranging from spare parts to major weapon systems such as fighter aircraft.[2]

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[2]The Department of Commerce, on the other hand, licenses "dual-use" items, which have both military and civilian commercial applications.

In order to apply for licenses to export defense articles controlled by OMC, the person or company must register with OMC. OMC's registration list includes manufacturers and freight forwarders as well as foreign governments. This list has increased nearly 40 percent in recent years from about 2,500 active registrants in 1984 to over 3,500 in 1987.

Once registered, an exporter may apply to OMC for an export license. When OMC receives a license application, it is recorded and assigned to one of five licensing officers. These officers are usually responsible for one or more categories of the Munitions Control List. The licensing officer examines each license application to determine if applicable legal, policy, security, regulatory, and procedural requirements have been satisfied. OMC's licensing officers have been provided with a number of regulatory, policy, and administrative guidelines to assist them in performing their duties. In general, they examine licenses to see whether the application involves items not licensed before or not previously licensed to a particular country or region, whether it is politically sensitive, or whether it involves sensitive technology.

In fiscal year 1986, OMC reported issuing licenses authorizing commercial exports valued at $14.9 billion (compared to $8.0 billion in U.S. government foreign military sales and grant assistance). Actual exports made under these licenses, which remain valid for 2 years, are considerably less than authorized. For example, in fiscal year 1984, OMC authorized $12.7 billion in

exports; according to OMC records, $3.8 billion was actually exported.

MOST LICENSE APPLICATIONS ARE ACTED ON IN 30 DAYS

According to OMC, it acted on over 49,000 applications in fiscal year 1986. Of these, OMC approved 90 percent (43,987), denied 2 percent (850) and returned 8 percent without action (4,181). A sample of license applications we examined showed similar results. Typically, license applications were denied because of concerns over the sensitivity of the technology and/or the destination country.

OMC officials told us that licensing officers can make decisions on most license applications quickly based on similar applications previously approved (precedents) and the licensing officer's familiarity with the parties and commodities involved. A recent OMC planning document stated that "[about] 80 percent of license applications can be acted on without review by other offices; most export authorizations are approved or denied by OMC within hours of receipt and returned to applicants within 2 weeks." We found that OMC processed (from receipt to final action) over three-fourths of the license applications it received in less than a month. Our random sample of 1,333 fiscal year 1986 applications showed that about 54 percent of these export license applications and other requests for OMC reviews were processed within 7 calendar days, about 71 percent within 14 days, and about 80 percent in 30 days. Less than 1 percent of the cases required more than 100 days.

As might be expected, the license applications that took the longest to review had been referred to other offices within the State Department or to other agencies for their recommendations on whether the license should be approved. This is an area OMC cannot totally control because it has to rely on other agencies to react. However, several industry representatives and DOD officials said that a number of license applications should not have been referred to DOD because the items involved had been previously approved for export or involved old technology.

The export license applications most likely to be sent out for recommendations involved either manufacturing licenses and technical assistance agreements, technical data, or selected hardware items involving sensitive technology. Factors affecting decisions to request recommendations included the lack of relevant precedents; questions about the proposed use, the contractors or intermediaries involved, or the destination country; or the licensing officer's lack of familiarity with the export item. New licensing officers are more likely to refer applications than experienced ones. OMC officials stressed that the ultimate decision over what cases are reviewed outside OMC rests with its licensing officers.

In our sample of fourth quarter fiscal year 1986 applications, 22 percent were sent to other agencies, most often to DOD and the services. Based on our sample, when OMC processed cases without asking for outside recommendations, 80 percent were completed within 7 calendar days. When recommendations were sought, 61

percent took over 30 days. For cases referred outside of OMC, we examined the processing time between key points in the review process. We found the following:

-- The time from receipt of cases in OMC to referral to other organizations ranged from 0 (same day) to 17 days. Eighty-six percent were referred within 9 days or less.

-- The time from referral to receipt of the last response ranged from 5 to 130 days. In 50 percent of the cases, the recommendations were received within 35 days or less.

-- The time from receipt of the last referral to final action in OMC ranged from 0 to 69 days. Final action on about 47 percent was completed within 8 days.

DOD's Defense Technology Security Administration (DTSA)--which formulates DOD's position on munitions exports--is working on an export application screening system which could be useful to OMC in identifying cases needing technical review. The system is also designed to screen application information against a series of reference data bases, including intelligence data pertaining to applicants and other parties to the license. The objective of the automated system is to (1) reduce the amount of routine work performed by DTSA staff, (2) reduce case processing time, and (3) improve the quality of case analysis by making pertinent data more accessible. DTSA officials indicated a willingness to share this system.

OMC's productivity plan focuses on timeliness

OMC's productivity plan for fiscal years 1987 to 1990--prepared in conjunction with State's participation in the Office of Management and Budget (OMB) management improvement initiatives--emphasizes the "important relationship between growing workload, static resources, and declining timeliness." OMC's plan calls for 15 additional full-time staff, temporary assignment of 2 military officers to OMC to help identify applications needing technical review, and improvements in the computer systems to speed up information retrieval. Most computer equipment (but not software) called for in the plan has been acquired, although three staff positions that were to be added in fiscal year 1988 were deleted from the State Department's request during OMB's review. The Executive Director of State's Bureau of Politico-Military Affairs told us that assignment of the military personnel was also unlikely.

LITTLE SCREENING OF REGISTRANTS AND LICENSE APPLICATIONS

OMC reviews registration forms only to be sure that all appropriate blocks are filled in. It does not verify the accuracy of information provided by registrants or use the information in licensing reviews other than to ensure that an applicant is registered.

Also, OMC does not systematically check parties to license applications (i.e., applicants, freight forwarders, and consignees) against lists of questionable exporters, exporters convicted of past export violations, or those denied export privileges by the

Department of Commerce. We found that OMC approved over 325 export licenses valued at about $15 million during fiscal year 1986 for a company denied export privileges by the Department of Commerce during the period. The company was denied export privileges for violation of the Export Administration Act.

Other agencies involved in munitions exports maintain information on export violators that could be used to identify license applications needing closer scrutiny in the review process. For example, Customs, which has primary munitions enforcement responsibility, keeps a listing of exporters convicted of violating export laws and regulations. The Chief of Customs' Strategic Investigations Division told us that this information could help OMC screen its registration list. However, he said that OMC had never asked Customs to screen the list, and his office had not done so because of its own resource limitations.

The Department of Commerce also maintains information from various sources regarding thousands of individuals and firms for which it has some enforcement concern. In a 1987 study, a Commerce Department official found that Commerce had negative information on approximately 26 percent of a random sample of OMC registrations. This official also found negative information on 27 percent of foreign consignees in a random sample of OMC licenses. The study did not categorize the negative information by degree of seriousness, such as separating known export violators from the subjects of less serious concerns. Thus, while this study was not sufficient to show that OMC should not have approved licenses, it

points out that screening applicants and other parties to license applications can help identify those applications potentially needing closer scrutiny.

OMC does not routinely use these lists nor has it developed one of its own. OMC officials said they have not formally developed lists of questionable firms and individuals out of concern that such lists would be subject to public disclosure under the Freedom of Information Act or disclosure to affected individuals under the Privacy Act. In the past, Commerce's General Counsel has ruled that such information is exempt from disclosure. As noted by Commerce, both acts cited by OMC provide that information may be exempted from disclosure for classification and law enforcement reasons.

Few checks to confirm end use

One way to verify application information is to ask the U.S. embassy in the destination country to check on the foreign parties to the application and try to determine whether the transaction appears legitimate. Of the approximately 49,000 license applications OMC received in fiscal year 1986, OMC officials estimated that they requested around 50 confirmation or end-use checks of application data by U.S. embassy staffs at the export destination point. OMC does not keep centralized files on those checks, and no checks were indicated in license files for the cases we sampled. Both the chief and deputy chief of OMC's Licensing Division expressed concern during our review about the limited number of end-use checks being made, yet we found no written

guidance which licensing officers would use to determine if an end-use check was warranted. According to OMC officials, resource limitations and the inability to identify questionable licenses quickly have limited the number of end-use checks requested of the embassies.

OMC authority to impose penalties

The State Department has authority to revoke licensing privileges, deny license requests based on prior export violations, and impose civil penalties. It has used this authority four times since 1976, the last time in November 1983. Of the four instances, one resulted in a debarment (60 days); the other three resulted in fines of $7,000, $10,000, and $120,000. Two of the exporters were penalized because items exported were diverted to a proscribed country. Information on the other two exporters was not readily available.

INSUFFICIENT FACILITIES AND CAPABILITIES TO STORE AND RETRIEVE DATA

OMC's capabilities for retrieving historical data that could be used in licensing reviews are limited. According to OMC and other State Department officials, OMC's facilities for data storage and its automated data processing capabilities are both insufficient to meet its needs.

Due in part to limited filing space and personnel resources, OMC's hard copy files contain little of the supporting data that is submitted with license applications. OMC sends case files to storage after a couple of years to accommodate newer files. In

1986, OMC obtained microfilm equipment to record and store data, but OMC had not started using it by the time we completed our fieldwork. OMC's automated data processing system contains only limited information, which is insufficient to be useful in analyzing precedents or to do other analyses of applications. Although the system contains case tracking information going back 6 to 7 years, it does not contain detailed information that could facilitate subsequent licensing decisions--such as commodity descriptions, foreign users or consignees, comments from other agencies, or provisos from earlier similar cases. Thus, licensing officers have to rely on hard copy files, which may not be readily available after a few years, and on their individual experience and knowledge.

OMC officials told us that limited automated data retrieval capabilities also result in the staff conducting time-consuming manual searches of OMC's records to support Customs' enforcement activities. For example, the staff manually searched OMC files back to 1981 to identify 300 cases relevant to one investigation. Further, the system does not contain specific item descriptions, foreign parties to the license application, and other details that could be used to identify possible criminal actions.

In our sample of the fourth quarter fiscal year 1986 applications, we identified precedents referenced on license applications and determined their availability within OMC. About half our sample cases cited one or more prior licenses as precedents. However, about 40 percent of them were no longer retained in OMC's active

files. Additionally, the precedent cases we found were not completely documented.

OMC has attempted to compensate for its lack of complete precedent data by asking applicants for it. In a newsletter dated September 1986, OMC alerted applicants that it would continue to retire records to make room for current cases and requested that they attach copies of precedent licenses and supporting documentation to new applications.

Long-term assessment is needed

The equipment improvements cited in OMC's productivity plan included upgrading OMC's computer system at a cost of $56,000, enhancing software design at a cost of $20,000, acquiring a microfilming system at a cost of $23,000, acquiring 14 new computer terminals at a cost of $93,000, and acquiring 5 printers at an unspecified cost. The computer and microfilming systems were purchased with fiscal year 1986 funds as were 5 of the 14 terminals. Funding for the software improvements is included in the fiscal year 1988 budget, but an OMC official said that he is hopeful they will be able to obtain funds from State Department's fiscal year 1987 supplemental appropriations. As of late August, this had not happened.

OMC's productivity plan provides an approach to meeting some immediate operational needs but is not based on a long-term needs assessment. In a memorandum dated August 14, 1985, State's Systems Design and Programming Division emphasized the need for long-range

automated data processing planning by OMC. The memorandum recommended that OMC not purchase a new computer until a thorough examination of its long-term requirements had been incorporated into an action plan--including budget scheduling and project phasing. The recommended plan would also include a requirements study and a feasibility and hardware analysis to form the basis for satisfying OMC's long-term needs.

OMC has not undertaken the recommended study nor has it enhanced its computer capabilities to address needs identified in the memorandum. OMC officials and licensing officers cited ways that increased automation could support both licensing and compliance activities. However, due to funding limitations, OMC does not plan to acquire additional software to broaden the system's functional capabilities until 1988. Even with the planned software improvements, the system will remain an automated filing system with little capability for automating the license review process.

COMPLIANCE WITH ADMINISTRATIVE REQUIREMENTS

OMC does not have adequate systems and procedures to ensure compliance with some regulatory requirements, including application documentation, reporting requirements, and return of licenses. OMC officials told us that they do not have sufficient resources to ensure that the requirements are met or to review required documentation and reports even when they are received. For example:

-- Most export license applications valued at or over $250,000 are supposed to have a letter stating whether political contributions and agents' fees were paid in connection with the sale. Our sample cases showed that for approved licenses for which such reports were required, 43 percent did not contain the required statement, nor were the license approvals conditioned on its receipt, which would have indicated an attempt to obtain information not submitted with the application.

-- OMC requires that licenses be returned after their use or on expiration. However, OMC does not know whether or not they have been returned. According to the Chief of OMC's Records and Reports Branch, many licenses are not returned to OMC in a timely manner--some are returned years after they should have been. He estimated that a quarter (tens of thousands annually) are not returned. We randomly selected 51 temporary export licenses for detailed examination and found that of those which were both approved and expired after 2 years, 67 percent were not in OMC's files indicating either they had not been returned or, if returned, were not properly filed. Either way, these expired licenses were not accounted for.

In addition, for manufacturing license agreement approvals, OMC requires annual reports of sales, including values and to whom sales were made. OMC's Deputy Director told us that they do not have sufficient staff to identify cases for which reports are required or to review the reports they receive.

OMC REPORTS UNDERSTATE THE VALUES AUTHORIZED AND ACTUAL EXPORTS

OMC reports on the value of exports authorized and actual exports differ markedly. The following table shows the differences between export data provided by OMC for fiscal years 1983 through 1986. We found that while numerous factors affect the accuracy of the figures, both are understated.

Table: OMC Reported Values of Authorized and Actual Exports

Category	Fiscal years			
	1983	1984	1985	1986
	(dollars in billions)			
Authorized exports	$8.7	$12.7	$9.9	$14.9
Actual exports	$4.0	$ 3.8	$2.3	$ 2.0
Difference (authorized minus actual)	$4.7	$ 8.9	$7.6	$12.9

The value of approved export licenses is understated

The value of OMC licenses authorizing commercial exports of defense articles and services is reported quarterly to the Congress. For fiscal year 1986, the reported value of such articles and services totaled $14.9 billion, which represents permanent exports of defense articles and related technology.

Not included in the reports are values associated with OMC cases for approval of various technical assistance agreements and manufacturing licenses authorizing foreign production. These cases may not cite specific dollar values, but when values are cited, they are not recorded in OMC's data base or reported to the Congress. Values cited for some agreement cases we examined ranged from minimal or none up to several millions of dollars.

OMC reports also do not include such values as those associated with repair services or replacement items that may be authorized for export by temporary import licenses which may have been used to return items to the United states for repair.

The value of actual exports is understated

OMC provides data on actual export values to the Defense Security Assistance Agency (DSAA), which includes the information in its annual reports on foreign military sales. A DSAA official has expressed concern that OMC's data is not verified, current, or compatible with other data in the report. Based on our assessment of the data, we agree.

Actual exports can lag behind approvals by as much as 2 years, since licenses are valid for that period of time, but other factors serve to make the actual export data incomplete. They center around Custom's processing of munitions export licenses and related documents, including Shipper's Export Declarations (SEDs). Customs sends OMC data on actual exports through SEDs indicating individual shipments against licenses and ultimately sends OMC expired licenses. However, SEDs may be incomplete and inaccurate and are not always returned to OMC.

Shipment values for a given year are subject to change as OMC updates its records with SEDs or returned licenses. However, OMC does not usually update prior years' values in its end-of-year reports to DSAA. OMC updated prior years' export values only at

the end of fiscal year 1985 when it updated export values for fiscal years 1983 and 1984. In doing so, the value of exports for fiscal year 1984 increased from $1.6 billion to $3.8 billion, and the value of exports for fiscal year 1983 increased from $2.4 billion to $4.0 billion. OMC cited limited computer resources as a reason for not updating prior years' export values for fiscal year 1986.

CONCLUSIONS

We recognize that budget limitations have imposed constraints on OMC. As its work load has increased, OMC appears to have placed greater emphasis on timeliness and less on detailed review of license applications. The near doubling of license applications in the last decade, combined with little growth in OMC resources, has meant that OMC has less time to review individual applications and ensure exporters' compliance with administrative and reporting requirements.

Even within tight constraints, OMC can improve its licensing operations. In order to focus its available resources, OMC could make better use of available information from other federal agencies to identify license applications needing closer scrutiny. Also, U.S. embassies could be tasked more frequently to provide checks on application information. These steps should not require any appreciable increase in resources, yet would provide greater assurance that license application data is accurate and the proposed sale is legitimate.

In the long term, much of OMC's license application review process can be automated. Detailed information on prior export licenses should be readily available to the licensing officers during their reviews. This information should include the types and amounts of munitions involved, the various parties to the transaction, and whether administrative requirements have been met, such as whether required reports were filed or an expired license has been returned. Information should also identify exporters and others who have previously violated export laws and regulations, who are currently under investigation, or who have been barred from making exports.

This concludes my prepared remarks. I will be happy to respond to any questions you may have.

INSTRUCTIONS FOR DSP-5

DOCUMENTS TO BE SUBMITTED WITH DSP-5

The following documentation is required for all license applications except for unshipped balances. Incomplete documentation will result in applications being returned without action.

a. For all hardware applications, one copy of a firm order or letter of intent must accompany the DSP-5. The firm order is usually a signed purchase contract. The letter of intent should be more than the purchaser's request for a proposal or submission of bids, and should indicate the purchaser's desire to buy the particular hardware cited on the application.

b. For all applications—hardware and technical data—over $250,000 for end-use by foreign armed forces, a letter or statement concerning political contributions and fees or commissions must accompany the DSP-5. If the political contributions are less than $5,000 and the fees or commissions less than $100,000, a statement similar to that effect is sufficient. Alternatively, a statement that no political contributions, fees, or commissions have been paid is acceptable. For political contributions of $5,000 or more, or fees or commissions of $100,000 or more, a detailed report, including a letter from the recipient, is required. (See 22 CFR 130 for details.) The amount of commission, rather than its description as a percentage of net profit, should be stated.

c. For all applications—hardware and technical data—for significant military equipment for $14 million or more for end-use by foreign armed forces, a statement should be submitted referring to the previous approval by the State Department in accordance with 22 CFR 126.8. 22 CFR 120.19 specifies which munitions list categories are significant military equipment.

d. For all hardware applications for significant military equipment, a Nontransfer and Use Certificate, Form DSP-83, must accompany the DSP-5. This document states that the commodity in question will not be transferred to any other party without State Department approval. It is to be signed by both the importer and the foreign end-user; the State Department may require the foreign government to sign the document if it is not the foreign end-user. The Office of Munitions Control reserves the right to require a Form DSP-83 for any request for export approval. (See 22 CFR 123.10.)

e. Supporting documentation, such as brochures, technical data, and spare parts/equipment lists, should be submitted in seven copies to cover staffing requirements. The need to submit such documentation should be decided on a case-by-case basis, if necessary, after a discussion with the Office of Munitions Control. Documentation will be necessary if the Office of Munitions Control and other reviewing offices and agencies do not have sufficient information on the hardware or technical data in question, or if the commodity description on the DSP-5 (block 9) or any other data requires amplification. Seven copies of continuation sheets or other attachments to the application are to be furnished in all cases.

f. For all firearms and firearm ammunition applications for commercial resale, an import permit from the government of the recipient country must be submitted.

g. Applicants who are freight forwarders must, for reasons of legal accountability, register with the Office of Munitions Control, submit a letter from the foreign embassy or company appointing them as forwarding agent, and submit a statement of responsibility that is in addition to the statement appearing in item 25 of the DSP-5. This supplemental declaration should certify that the articles shown on the export application they submit are, from their personal knowledge, in fact the articles by quantity, type, and value to be exported.

GENERAL INSTRUCTIONS

a. Do not use this form for equipment or technical data bearing a U.S. military security classification. A DSP-85 should be used instead.

b. For hardware shipments, a separate application is required for each country of export in order to maintain a clear record of the shipment and end-use of the equipment.

c. For technical data exports, several countries may be listed in item 3. However, as a general rule, when the countries of ultimate destination are geographically dispersed, it is advisable to submit a separate application for countries in each geographical region (e.g., Africa; East Asia; Europe, etc.). PM/MC licensing officers will provide guidance on specific cases upon request.

d. Carbon paper is necessary but should be removed after completion. Applications should be typed. Please do not remove the tab (the snap-out top portion of the DSP-5).

e. All items must be answered, if necessary, by stating "none" or "same as item _____," rather than leaving a space blank.

f. Documentation submitted by the company to be returned should be stamped "RETURN TO SENDER" on each copy.

g. 22 CFR 123.25(d) states that Customs authorities may authorize hardware shipments where the value has increased beyond that stated on the license, but by no more than 10 percent.

h. The license application and supporting documents should be sent to: Office of Munitions Control, PM/MC, Room 800, SA-6, Department of State, Washington, D.C. 20520.

i. Reproductions of approved licenses may be made for recordkeeping purposes only, not for making shipments.

SPECIFIC GUIDELINES

Item 4: The known or probable initial U.S. port of exit, rather than a more general statement such as "any east coast port," should be entered.

Item 5: The parent corporation must be shown on the first line. If desired, a subsidiary company or division may be placed under the name of the parent corporation.

Item 9: List each commodity clearly, giving type, model number, catalog number, or make, to aid in identification. When applicable, give the military designation and U.S. Government contract numbers. When components and spare parts are involved, fully identify the minor component, major component, and end item in which they will be used (e.g., turbine blades for _____ jet engine for _____ aircraft). If the hardware is being furnished under an approved licensing agreement, give the PM/MC case number.

Item 11: Values for hardware should include the selling price without supplementary costs such as packing and freight. Values for technical data can be the selling price or procurement cost, as appropriate.

Item 13: Specify, in addition to the source or manufacturer of the commodity, whether the material is new, or used, or acquired from U.S. Government surplus.

Item 16: Show who will deliver the commodity to the foreign consignee or intermediate consignee.

Item 18: 22 CFR 123.9 requires that the country designated on a license application as the country of ultimate destination must be the country in which the exported defense articles, related technical data, or defense services will receive ultimate end-use. Furthermore, such articles, data, and services shall not be transferred by any means to a national of another country or to any other country without the prior written approval of the Office of Munitions Control. In the absence of end-use information from the foreign customer, applicants must not assume that the end-user is the firm that placed the order or the government of that country. End-use must be ascertained before applying for licenses. All DSP-5 hardware applications must be accompanied by the customer's end-use confirmation on the purchase order, telex, or other supporting documentation.

Item 19: The foreign intermediate consignee does not refer to banks or common carriers.

Item 20: If the transaction includes both an unshipped balance from a previous license and new orders, two separate applications are required.

(DEPARTMENT OF STATE USE ONLY)

SEAL

Signature

License hereby granted to applicant for described commodity to be permanently exported from the United States. This license may be revoked, suspended, or amended by the Secretary of State without prior notice whenever the Secretary deems such action advisable.

LICENSE NO.

LICENSE VALID FOR 24 MONTHS FROM ABOVE DATE

UNITED STATES OF AMERICA — DEPARTMENT OF STATE

APPLICATION/LICENSE FOR PERMANENT EXPORT OF UNCLASSIFIED DEFENSE ARTICLES AND RELATED UNCLASSIFIED TECHNICAL DATA

1. Date Prepared	2. PM/MC Applicant Code	3. Country of Ultimate Destination	4. Probable Port of Exit from U.S.

5. Applicant's Name, Address, ZIP Code, Tel. No.

TELEPHONE NUMBER:

6. Names, agency, and telephone numbers of U.S. Government personnel (not PM/MC) familiar with the commodity

7. Name and telephone number of applicant contact if U.S. Government needs additional information.

8. QUANTITY	9. COMMODITY (Follow instructions carefully)	10. MUNITIONS LIST CATEGORY	11. VALUE
	☐ Hardware ☐ Technical Data		

12. TOTAL VALUE: $

13. Source or Manufacturer of Commodity

14. Specific purpose for which the material is required, including specific program/end item

15. Name and Address of Seller in United States

16. Name and Address of Consignor in United States

17. Name and Address of Foreign Consignee

18. Name and Address of Foreign End User

19. Name and Address of Foreign Intermediate Consignee

20. This application represents: ☐ ONLY completely new shipment; ☐ ONLY the unshipped balance of license no. _____
NOTE: APPLICATION CANNOT INCLUDE BOTH

21. The IDENTICAL commodity ☐ was licensed to the country in block 3 under license no. _____, ☐ was licensed to other countries under license no. _____; ☐ was denied to the country in block 3 under voided license no. _____, ☐ never licensed for this applicant

22. If commodity is being provided under a Foreign Military Sales (FMS) or Grant Aid (GAD) program, state which _____ and give the case no. _____

23. In this transaction, applicant is: ☐ government ☐ agent/manufacturer ☐ freight forwarder

24. LICENSE TO BE SENT TO: Name, Address, ZIP Code

25. APPLICANT'S STATEMENT (See Instructions)

I, _____ (TYPED NAME), hereby apply for a license to complete the transaction described above; warrant the truth of all statements made herein; and acknowledge, understand, and will comply with the provisions of Title 22 CFR 120-130 and any conditions and limitations imposed.

Signature _____

FORM DSP-5
4/98

1—APPLICATION/LICENSE

FORM APPROVED
OMB NO. 1405-0003
EXP. DATE: 6/1/98

APPROVED LICENSE MUST BE PRESENTED TO U.S. CUSTOMS OR POST OFFICE PRIOR TO EXPORT/MAILING

CONDITIONS OF ISSUANCE

1. A license to export articles on the U.S. Munitions List is issued under the conditions cited in 22 CFR 120-130, including the provisos, as applicable, that:
   A. It shall not be construed as implying U.S. Government approval or commitment to authorize future exports of any article (equipment or technical data) on the Munitions List, or any U.S. Government commitment with regard to any proposed manufacturing license or technical assistance agreements which may result from an authorized export.
   B. If a license is issued for technical data only it does not authorize the export of any equipment; if a license is issued for equipment only it does not authorize the export of any technical data unless specifically covered by an exemption in 22 CFR 125.4.
   C. The applicant's commitments to the U.S. Government are being met.
2. The issuance of this license does not release the license from complying with other requirements of U.S. law and regulations.
3. The prior written approval of the Department of State must be obtained before U.S. Munitions List articles exported from the U.S. under license may be resold, diverted, transferred, transshipped, reshipped, or reexported to or used in any country other than that described on the license as the country of ultimate destination.

RETURN OF LICENSE

This license must be returned to the Office of Munitions Control, Department of State, Washington, DC 20520 when: (1) the total value authorized has been shipped; (2) the applicant states that there will be no further shipments; (3) the date of expiration is reached; or (4) when requested by the Office of Munitions Control.

CUSTOMS AND POSTAL ENDORSEMENT

Indicate below which *ITEM* on the face of the license is *BEING EXPORTED* and maintain a *CONTINUING BALANCE* of the remaining value.

QUANTITY	COMMODITY	SHIPMENT VALUE	DATE	SED NO.	OFFICER INITIALS	PORT OF EXIT NAME OR NO.
	TOTAL AUTHORIZED					
	REMAINING BALANCE					
	REMAINING BALANCE					
	REMAINING BALANCE					

United States General Accounting Office

GAO

Report to the Chairman, Subcommittee on Federal Services, Post Office, and Civil Service, Committee on Governmental Affairs, U.S. Senate

September 1987

ARMS EXPORTS

Licensing Reviews for Exporting Military Items Can Be Improved

GAO/NSIAD-87-211

GAO

United States
General Accounting Office
Washington, D.C. 20548

National Security and
International Affairs Division

B-228821

September 9, 1987

The Honorable David H. Pryor
Chairman, Subcommittee on Federal
Services, Post Office, and Civil Service
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

On March 23, 1987 you requested that we review arms export licensing by the Department of State's Office of Munitions Control (OMC). Specifically, you asked us to examine OMC's licensing activities and procedures, including timeliness and exporter compliance with certain administrative and reporting requirements. You also asked us to identify actions OMC is taking to cope with its increased work load. Because the documentation associated with licensing reviews was not readily available, we did not examine whether licenses were improperly granted. We also did not examine whether munitions were improperly exported.

The United States transfers military items and services overseas in two major ways: (1) U.S. government sales and grants under the Foreign Military Sales Program and the Military Assistance Program, respectively, and (2) commercial arms sales by individuals and business entities. For the latter category of sales, the exporter must have a U.S. government export license approved by OMC. OMC issues export licenses for items which are inherently military in nature, ranging from spare parts to major weapon systems such as fighter aircraft.[1] The Department of Defense (DOD) assists OMC by performing technical reviews of many license applications and providing advice on national security considerations. During our review of OMC, we touched on DOD activities but did not evaluate DOD's performance or effectiveness.

In fiscal year 1986, OMC reported issuing licenses authorizing commercial exports valued at $14.9 billion (compared to $8.0 billion in U.S. government foreign military sales and grant assistance). Actual exports made under these licenses, which remain valid for 2 years, are considerably less than authorized. For example, in fiscal year 1984, OMC authorized $12.7 billion in exports; according to OMC records, $3.8 billion was actually exported.

[1]The Department of Commerce, on the other hand, licenses "dual-use" items, which have both military and civilian commercial applications.

During fiscal year 1986, OMC approved about 90 percent of the license applications it acted on. Based on a sample of those applications, over 80 percent were acted on in less than a month. However, we also found that

- Export license application data and information were not routinely checked for accuracy or veracity. OMC rarely requested U.S. embassies' assistance in verifying the bona fides of the purchaser or other foreign parties to the sale. OMC also was not using readily available information about exporters and others involved in commercial sales transactions that would help identify applications potentially needing closer scrutiny. For example, OMC did not use U.S. Customs or Department of Commerce listings of individuals and companies previously convicted of violating export laws or denied export privileges.
- OMC's facilities and automated capabilities are insufficient for storing and quickly retrieving historical data which would be useful in license application reviews, such as detailed data on prior export licenses that are cited by applicants as precedents. Many of the application files we looked for had been sent to storage or the documentation attached was incomplete. The review process has remained largely manual rather than automated. OMC's computer system is basically an automated filing system of limited capacity and has little additional capability.
- OMC's systems and procedures are not adequate to ensure compliance with some administrative and reporting requirements. For example, over 40 percent of the export license applications in our sample that should have had statements concerning political contributions or agents' fees, did not. Additionally, export licenses are supposed to be returned to OMC after their use or when they expire. OMC does not know whether it has the licenses or not. Based on a judgmental sample, two-thirds of the licenses that should have been returned could not be found.

OMC officials stated that an increased work load and static resources have restricted their application review efforts, including their ability to ensure compliance with all administrative requirements. OMC's volume of munitions cases (license applications and other requested approvals) has increased from about 26,000 in 1977 to over 49,000 in 1986 and is expected to exceed 52,000 in fiscal year 1987. Over the same period, OMC's staff has remained at around 30 persons with 10 staff members authorized to approve licenses. OMC has prepared a plan to increase staffing levels and improve its automated systems, but important features of the plan are likely to be curtailed due to budget limitations.

To help ensure that technical, national security, and foreign policy concerns are considered, OMC sends license applications which require additional scrutiny to other federal agencies, principally DOD. DOD's Defense Technology Security Administration, the entity that coordinates and formulates DOD's reviews, is developing an automated system designed to help identify licenses needing closer review. The system is also supposed to screen license applications against a series of data bases, including intelligence data, that should help identify those applications involving applicants and other parties with a history of wrongdoing, which may need closer scrutiny. Such a system should help OMC licensing officers decide which applications should be referred to DOD, and DOD officials have indicated a willingness to share the system with OMC.

Conclusions and Recommendations

We recognize that budget limitations have imposed constraints on OMC. As its work load has increased, OMC appears to have placed greater emphasis on timeliness and less on detailed review of license applications. The near doubling of license applications in the last decade, combined with little growth in OMC resources, has meant that OMC has less time to review individual applications and ensure exporters' compliance with administrative and reporting requirements.

Even within tight constraints, OMC can improve its licensing operations. In order to focus its available resources, OMC could make better use of available information from other federal agencies to identify license applications needing closer scrutiny. Also, U.S. embassies could be tasked more frequently to provide checks on application information. These steps should not require any appreciable increase in resources, yet would provide greater assurance that license application data is accurate and the proposed sale is legitimate.

In the long term, much of OMC's license application review process can be automated. Detailed information on prior export licenses should be readily available to the licensing officers during their reviews. This information should include the types and amounts of munitions involved, the various parties to the transaction, and whether administrative requirements have been met, such as whether required reports were filed or an expired license has been returned. Information identifying exporters and others who have previously violated export laws and regulations, are currently under investigation, or barred from making exports should also be included.

Accordingly, we are recommending that the Secretary of State require OMC to

- use readily available information on parties involved in arms exports to help identify export license applications requiring closer scrutiny,
- develop procedures and criteria for requesting that U.S. embassies help verify license application information, and
- ensure exporter compliance with administrative and reporting requirements.

To minimize the effect of the above actions on OMC's timeliness, we are also recommending that OMC assess its long-term automation needs with a view towards automating much of the export license review process. In this connection, OMC should examine the feasibility of adapting for its use the automated review system being developed by DOD.

Appendix I contains detailed information on our findings and recommendations and a discussion of our objectives, scope, and methodology. We discussed this report with cognizant agency officials and have included their comments where appropriate. As requested, we did not obtain written comments.

Unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its issue date. At that time we will send copies of the report to other interested congressional committees; the Secretaries of State, Defense, Commerce, and Treasury; the Director, Office of Management and Budget; and other interested parties.

Sincerely yours,

Frank C. Conahan

Frank C. Conahan
Assistant Comptroller General

Appendix I

The Office of Munitions Control Can Strengthen Its License Review Process

The Arms Export Control Act (AECA), 22 U.S.C. 2778, 2794 (1982), provides legislative authority for regulating the commercial export of defense articles and services and related technical data. The defense articles and services subject to export control and the requirements which must be met in order to export those items are set forth in the International Traffic in Arms Regulations (ITAR), 22 C.F.R., parts 121-130. Executive Order 11958, dated January 18, 1977, assigned responsibility for controlling the commercial export of military items to the Secretary of State. Within the Department of State, that function is assigned to the Office of Munitions Control (OMC), which is part of State's Bureau of Politico-Military Affairs.

OMC's Organization and Responsibilities

To carry out its responsibilities, OMC has a staff of about 30. OMC is headed by a career service director, a deputy director, and two special assistants. It is organized into two operating divisions—the Licensing Division and the Processing Control Division. At the time of our review, the Licensing Division was staffed by a chief, a deputy chief, five licensing officers, and support staff. The managers and licensing officers are responsible for reviewing the applications to determine if all legal, policy, and procedural requirements are met and deciding whether to grant the license. In addition to the Licensing Division staff, OMC's director, deputy director, and one of the special assistants often perform license review functions, including granting approvals.

The remainder of OMC's personnel are in its Processing Control Division, which provides the administrative, record keeping, filing, data entry, and processing functions in support of the Licensing Division. The division chief and two paralegal analysts perform what OMC refers to as compliance work. OMC officials describe their compliance activities as primarily supporting the U.S. Customs Service and the Department of Justice in their efforts to ensure that munitions exports are properly licensed and that violations are investigated and prosecuted. For the most part, this support involves searching OMC's files for records relevant to investigations and occasionally providing expert testimony in court.

The License Process

The ITAR stipulates that with certain exceptions any person, firm, or other organization (including foreign governments) that "engages in the United States in the business of either manufacturing or exporting defense articles or furnishing defense services is required to register

with the Office of Munitions Control." In practical terms, OMC's registration list includes manufacturers and freight forwarders as well as foreign governments that, once registered, may apply for export licenses. A registrant provides OMC with information concerning the organization, including its principal officers and foreign subsidiaries, the nature of its business, and commodities in which it deals. A registrant may register for up to 5 years. OMC's registration list has increased nearly 40 percent in recent years from about 2,500 active registrants in 1984 to over 3,500 in 1987.

Once registered, an exporter may apply to OMC for an export license. When OMC receives a license application the application is recorded and assigned to one of OMC's five licensing officers. These officers are usually responsible for one or more categories of the Munitions Control List. The licensing officer examines each license application to determine if applicable legal, policy, security, regulatory, and procedural requirements have been satisfied. OMC's licensing officers have been provided with a number of regulatory, policy, and administrative guidelines to assist them in performing their licensing duties. In general, they examine licenses to see whether the application involves items not licensed before or not previously licensed to a particular country or region, whether it is politically sensitive, or whether it involves sensitive technology.

Since licensing officers are not policy or technical experts, they may also refer applications to other federal agencies, such as the Department of Defense (DOD), the Arms Control and Disarmament Agency, the National Aeronautics and Space Administration, or other bureaus within the Department of State, for technical or policy reviews before making a licensing decision. For example, an application to export a weapon system might be referred to DOD, while the export of small arms where human rights conditions are of concern might be referred to State's regional bureaus and its Bureau of Human Rights and Humanitarian Affairs.

After any referrals are completed, the licensing officers will approve, deny, or return the license without action. The latter is usually for administrative deficiencies, such as incomplete information, or obvious denials, such as where exporting the particular item to the destination country is prohibited by law.

An approved license is generally valid for 2 years up to the limits on quantity and value specified on the license. The exporter presents the

license to the U.S. Customs Service District Director for the port of export. Customs holds the license until the export is completed and has the responsibility to record exports as they leave the United States and send OMC the documentation of the quantity and value of the actual shipments. When the license expires or the approved export is completed, Customs is supposed to return the license to OMC. These returned licenses allow OMC to compare actual exports to the quantities authorized. As discussed in a later section, OMC data shows that actual exports are significantly less than authorized licensed quantities.

Kinds of Licenses

OMC reviews several categories of export license applications and other requests not specifically identified as licenses. These include applications or requests to

- permanently export defense articles and services and related technical data;
- temporarily export defense items, such as taking a weapon system to an overseas trade show and planning to return it to the United States;
- temporarily import defense items, such as returning an item for repairs in the United States and planning to reexport it;
- enter into agreements to authorize or license the manufacture of defense articles abroad (can include the export of technical data or defense articles);
- perform defense services or disclose technical data abroad; and
- retransfer defense articles previously approved for export.

OMC also provides opinions concerning the need for OMC licensing and advisory opinions on the likelihood of OMC approving a particular export. Table I.1 indicates OMC's work load during fiscal years 1983 through 1986. OMC officials estimate that the fiscal year 1987 work load will exceed 52,000 cases.

Table I.1: Cases Received by OMC

	Fiscal year			
Case type	**1983**	**1984**	**1985**	**1986**
Permanent exports	30,947	35,043	33,315	35,743
Temporary imports	3,631	4,339	4,857	5,885
Temporary exports	3,088	4,144	3,841	4,419
Classified transactions	668	811	589	606
Agreements	880	956	1,157	1,391
Other[a]	1,358	1,148	1,089	1,121
Total[b]	**40,572**	**46,441**	**44,848**	**49,165**

Source: OMC

[a]Primarily advisory opinions and requests for determination of whether OMC licenses were needed.

[b]These totals represent cases recorded as received at OMC. OMC officials told us that some cases are returned to applicants without being recorded because of obvious deficiencies, such as not being complete. OMC estimates the number of such cases at a few hundred per year. OMC does not maintain records on these cases.

Types of Items Being Licensed

To gain an understanding of the nature of the license applications OMC receives, we randomly sampled OMC permanent export licenses (which are over 70 percent of OMC's license reviews) for the fourth quarter of fiscal year 1986. OMC reviews export license applications for a great variety of munitions items—from a single handgun to a fighter aircraft—and technical data packages. Based on our sample, export license applications are usually for hardware items (86 percent) and involve parts and components rather than major weapon systems. Technical data packages accounted for about 12 percent in our sample; the remaining 2 percent were a mixture of hardware and technical data. Nearly 80 percent of our sample applications with commodity values reported (some did not have a value reported) were valued at $100,000 or less with more than half valued at less than $10,000.

Most License Applications Are Acted on in 30 Days

According to OMC, it acted on over 49,000 applications in fiscal year 1986. Of these, OMC approved 43,987 (90 percent), denied 850 (2 percent), and returned 4,181 without action (8 percent). Our sample showed similar results. Typically license applications were denied because of concerns over the sensitivity of the technology and/or the destination country.

OMC officials told us that licensing officers can make decisions on most license applications quickly based on similar applications previously approved (precedents) and the licensing officer's familiarity with the

parties and commodities involved. A recent OMC planning document stated that "[about] 80 percent of license applications can be acted on without review by other offices; most export authorizations are approved or denied by OMC within hours of receipt and returned to applicants within 2 weeks." We found that OMC processed (from receipt to final action) over three-fourths of the license applications it received in less than a month. Our random sample of 1,333 fiscal year 1986 applications showed that about 54 percent of the export license applications and other requests for OMC reviews were processed within 7 days,[1] about 71 percent within 14 days, and more than 80 percent in 30 days. Less than 1 percent of the cases required more than 100 days.

As might be expected, the license applications that took the longest to review had been referred to other offices within the State Department or to other agencies for their recommendations on whether the license should be approved. License applications referred to other agencies receive additional scrutiny from foreign policy and/or national security standpoints, including technical perspectives.

The export license applications most likely to be sent out for recommendations involved either manufacturing licenses and technical assistance agreements, technical data, or selected hardware items involving sensitive technology. Factors affecting decisions to request recommendations included the lack of relevant precedents; questions about the proposed use, the contractors or intermediaries involved, or the destination country; or the licensing officer's lack of familiarity with the export item. New licensing officers are more likely to refer license applications than experienced ones. OMC officials stressed that the ultimate decision over what cases are reviewed outside OMC rests with its licensing officers.

In our sample of fourth quarter fiscal year 1986 applications, 22 percent were sent to other agencies, most often to DOD and the services. Table I.2 contrasts the processing time for the fourth quarter applications in our sample sent for recommendations as opposed to those that were not.

[1] All the time frame calculations in our sample are in calendar days.

Table I.2: Case Processing Time

Completion time (calendar days)	Percent		
	Cases sent out[a]	Cases not sent out[b]	Total cases[c]
0-1	3	23	19
2-7	6	57	46
8-21	17	14	15
22-30	14	1	4
31-45	17	1	4
46-60	14	2	4
61-100	25	1	6
101+	6	2	2

[a]Percentages are based on the fourth quarter sample cases referred to others for comment. Percentages do not add to 100 due to rounding.

[b]Percentages are based on the fourth quarter sample cases that were not sent for recommendations.

[c]Percentages are for our sample of fourth quarter permanent export license applications.

OMC's Productivity Plan Focuses on Timeliness

OMC's productivity plan for fiscal years 1987 to 1990—prepared in conjunction with State's participation in the Office of Management and Budget (OMB) management improvement initiatives—emphasizes the "important relationship between growing workload, static resources, and declining timeliness." OMC's plan calls for 15 additional full-time staff, temporary assignment of 2 military officers to OMC to help identify applications needing technical review, and improvements in the computer systems to speed up information retrieval. Most computer equipment (but not software) called for in the plan has been acquired, although three staff positions that were to be added in fiscal year 1988 were deleted from the State Department's request during OMB's review. The Executive Director of State's Bureau of Politico-Military Affairs told us that assignment of the military personnel was also unlikely.

As illustrated above, cases referred for recommendation take longer to be acted on; this is an area OMC cannot totally control because it has to rely on other agencies to react. However, several industry representatives and DOD officials said that a number of license applications should not have been referred to DOD because the items involved had been previously approved for export or involved old technology.

DOD's Defense Technology Security Administration (DTSA)—which formulates DOD's position on munitions exports—is working on an export application screening system which could be useful to OMC in identifying

cases needing DOD's technical review. The system is also designed to screen application information against a series of reference data bases, including intelligence data pertaining to applicants and other parties to the license. The objective of the automated system is to (1) reduce the amount of routine work performed by DTSA staff, (2) reduce case processing time, and (3) improve the quality of case analysis by making pertinent data more accessible. DTSA officials indicated a willingness to share this system.

Little Screening of Registrants and License Applications

OMC reviews registration forms only to be sure that all appropriate blocks were filled in. It does not verify the accuracy of information provided by registrants or use the information in licensing reviews other than to ensure that an applicant is registered.

Also, OMC was not systematically checking parties to license applications (i.e., applicants, freight forwarders, and consignees) against lists of questionable exporters, exporters convicted of past export violations, or those denied export privileges by the Department of Commerce. We found that OMC approved 325 export licenses valued at about $15 million during fiscal year 1986 for a company denied export privileges by the Department of Commerce during the period. The company was denied export privileges for violation of the Export Administration Act.

Other agencies involved in munitions exports maintain information on export violators that could be used to identify license applications needing closer scrutiny in the review process. For example, Customs, which has primary munitions enforcement responsibility, keeps a listing of exporters convicted of violating export laws and regulations. The Chief of Customs' Strategic Investigations Division told us that this information could help OMC screen its registration list. However, he said that OMC had never asked Customs to screen the list, and his office had not done so because of its own resource limitations.

Officials in DOD and Customs consider the use of such information to be an important tool for license application reviews. A DOD official told us that hundreds of individuals and firms should be considered questionable. The munitions export license applications they submit should be carefully reviewed to help insure the transaction is legitimate and conforms with U.S. arms export policies.

Similarly, the Department of Commerce also maintains information indicating concerns from various sources regarding thousands of individuals

and firms for which it has some enforcement concern. In a 1987 study, a Commerce Department official found that Commerce had negative information on approximately 26 percent of a random sample of OMC registrations. This official also found negative information on 27 percent of foreign consignees in a random sample of OMC licenses. The study did not categorize the negative information by degree of seriousness, such as separating known export violators from the subjects of less serious concerns. Thus, while this study was not sufficient to show that OMC should not have approved licenses, it points out that screening applicants and other parties to license applications can help identify those applications potentially needing closer scrutiny.

OMC officials said that they were aware of less than 30 questionable firms or individuals. They have not formally developed lists of questionable firms and individuals out of concern that such lists would be subject to public disclosure under the Freedom of Information Act[2] or disclosure to affected individuals under the Privacy Act.[3] In the past, Commerce's General Counsel has ruled that such information is exempt from disclosure. As noted by Commerce, both acts cited by OMC provide that information may be exempted from disclosure for classification and law enforcement reasons.

Few Checks to Confirm End Use

One way to verify application information is to ask the U.S. embassy in the destination country to check on the foreign parties to the application and try to determine whether the transaction appears legitimate. Of the approximately 49,000 license applications OMC received in fiscal year 1986, OMC officials estimated that they requested around 50 confirmation or end-use checks of application data by U.S. embassy staffs at the export destination point. OMC does not keep centralized files on those checks, and no checks were indicated in license files for the cases we sampled. Both the chief and deputy chief of OMC's Licensing Division

[2]The Freedom of Information Act provides agencies with several exemptions for withholding information from public disclosure. These include exemptions for classified information and for information the disclosure of which could reasonably be expected to interfere with enforcement proceedings (5 U.S.C.A. 552(b)(1) and (7), 1987).

[3]Under the Privacy Act, 5 U.S.C. 552a, an individual may have access to records and information pertaining to him in an agency's system of records, which is maintained by personal name or other individual identifier (e.g., Social Security Number), 5 U.S.C. 552a(d). Classified information may be exempt from disclosure (5 U.S.C. 552a(k)(1)). Investigatory material compiled for law enforcement purposes may also be exempted from such disclosures, except when it results in the denial of any benefit, privilege, or right to which an individual is entitled under federal law (5 U.S.C. 552a(k)(2)). No court cases have been reported which define whether an export license is a benefit, privilege, or right under this section.

expressed concern during our review about the limited number of end-use checks being made, yet we found no written guidance which licensing officers would use to determine if an end-use check was warranted. According to OMC officials, resource limitations and the inability to identify questionable licenses quickly limit the number of end-use checks that are being requested of the embassies.

OMC Authority to Impose Penalties

The State Department has authority to revoke licensing privileges, deny license requests based on prior export violations, and impose civil penalties. It has used this authority four times since 1976, the last time in November 1983. Of the four instances, one resulted in a debarment (60 days); the other three resulted in fines of $7,000, $10,000, and $120,000. Two of the exporters were penalized because items exported were diverted to a proscribed country. Information on the other two exporters was not readily available.

Insufficient Facilities and Capabilities to Store and Retrieve Data

OMC's capabilities for retrieving historical data that could be used in licensing reviews are limited. According to OMC and other State Department officials, OMC's facilities for data storage and its automated data processing capabilities are both insufficient to meet its needs.

Due in part to limited filing space and personnel resources, OMC's hard copy files contain little of the supporting data that is submitted with license applications. OMC sends case files to storage after a couple of years to accommodate newer files. In 1986, OMC obtained microfilm equipment to record and store data, but OMC had not started using it by the time we completed our fieldwork. OMC's automated data processing system contains only limited information, which is insufficient to be useful in analyzing precedents or to do other analyses of applications. Although the system contains case tracking information going back 6 to 7 years, it does not contain detailed information such as commodity descriptions, foreign users or consignees, comments from other agencies, or provisos from earlier similar cases that could facilitate subsequent licensing decisions. Thus, licensing officers have to rely on hard copy files, which may not be readily available after a few years, and on their individual experience and knowledge.

OMC officials told us that OMC's limited automated data retrieval capabilities also result in OMC staff conducting time-consuming manual searches of its records to support Customs' enforcement activities. For example, OMC staff manually searched OMC files back to 1981 to identify 300 cases

relevant to one investigation. Further, the system does not contain specific item descriptions, foreign parties to the license application, and other details that could be used to identify possible criminal actions.

In our sample of the fourth quarter fiscal year 1986 applications, we identified precedents referenced on license applications and determined their availability within OMC. About half our sample cases cited one or more prior licenses as precedents. However, about 40 percent of them were no longer retained in OMC's active files. Additionally, the precedent cases we found were not completely documented.

OMC has attempted to compensate for not having complete precedent data by asking applicants for it. In a newsletter dated September 1986, OMC alerted applicants that it would continue to retire records to make room for current cases and requested that they attach copies of precedent licenses and supporting documentation to new applications.

Long-Term Assessment Is Needed

The equipment improvements cited in OMC's productivity plan included upgrading OMC's computer system at a cost of $56,000, enhancing software design at a cost of $20,000, acquiring a microfilming system at a cost of $23,000, acquiring 14 new computer terminals at a cost of $93,000, and acquiring 5 printers at an unspecified cost. The computer and microfilming systems were purchased with fiscal year 1986 funds as were 5 of the 14 terminals. Funding for the software improvements is included in the fiscal year 1988 budget, but an OMC official said that he is hopeful they will be able to obtain funds from State Department's fiscal year 1987 supplemental appropriations. As of late August, this had not happened.

OMC's productivity plan provides an approach to meeting some immediate operational needs but is not based on a long-term needs assessment. In a memorandum dated August 14, 1985, State's Systems Design and Programming Division emphasized the need for long-range automated data processing planning by OMC. The memorandum recommended that OMC not purchase a new computer until a thorough examination of its long-term requirements had been incorporated into an action plan—including budget scheduling and project phasing. The recommended plan would also include a requirements study and a feasibility and hardware analysis to form the basis for satisfying OMC's long-term needs.

OMC has not undertaken the recommended study nor has it enhanced its computer capabilities to address needs identified in the memorandum.

OMC officials and licensing officers cited ways that increased automation could support both licensing and compliance activities. However, due to funding limitations, OMC does not plan to acquire additional software to broaden the system's functional capabilities until 1988. Even with the planned software improvements, the system will remain an automated filing system and has little capability for automating the license review process.

Compliance With Administrative Requirements

OMC does not have adequate systems and procedures to ensure compliance with some regulatory requirements, including application documentation, reporting requirements, and return of licenses. OMC officials told us that they do not have sufficient resources to ensure that the requirements are met or to review required documentation and reports even when they are received. For example:

- Most export license applications valued at or over $250,000 are supposed to have a letter identifying whether political contributions and agents' fees were paid in connection with the sale. Our sample cases showed that for approved licenses for which such reports were required, 43 percent did not contain the required statement, nor were the license approvals conditioned on its receipt, which would have indicated an attempt to obtain information not submitted with the application.
- OMC requires that licenses be returned after their use or on expiration. However, OMC does not know whether or not they have been returned. According to the Chief of OMC's Records and Reports Branch, many licenses are not returned to OMC in a timely manner—some are returned years after they should have been. He estimated that a quarter (tens of thousands annually) are not returned. We randomly selected 51 temporary export licenses for detailed examination and found that of those which were both approved and expired after 2 years, 67 percent were not in OMC's files indicating either they had not been returned or, if returned, were not properly filed. Either way, these expired licenses were not accounted for.

In addition, for manufacturing license agreement approvals, OMC requires annual reports of sales, including values and to whom sales were made. OMC's Deputy Director told us that they do not have sufficient staff to identify cases for which reports are required or to review the reports they receive.

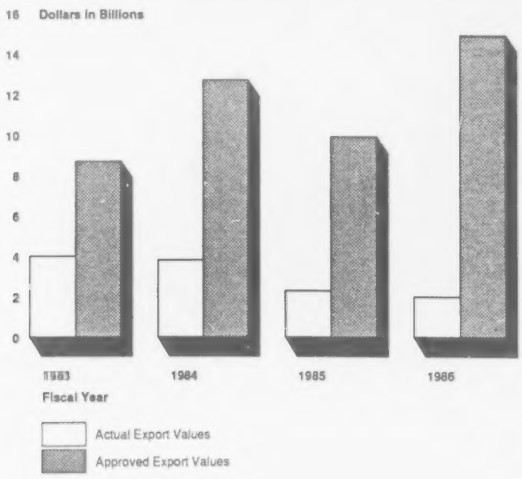
OMC Reports Understate the Values Authorized and Actual Exports

OMC reports on the value of exports authorized and actual exports differ markedly. Figure I.1 shows the difference between export data provided by OMC for fiscal years 1983-86. We found that while numerous factors affect the accuracy of the figures, both are understated.

The Value of Approved Export Licenses Is Understated

Section 36(a) of the AECA requires quarterly reports to Congress on the value of OMC licenses authorizing commercial exports of defense articles and services. For fiscal year 1986, the reported value of such articles and services totaled $14.9 billion, which represents permanent exports of defense articles and related technology.

Figure I.1: Values for Approved Licenses and Actual Exports Reported by OMC



Not included in the reports are values associated with OMC cases for approval of various technical assistance agreements, which often provide for export of defense services, and manufacturing licenses authorizing foreign production. These cases may or may not cite specific dollar values, but these amounts are not recorded in OMC's data base or reported to the Congress. Values cited for some agreement cases we examined ranged from minimal or none up to several millions of dollars. According to OMC officials, manufacturing licenses and technical assistance agreements can cover a period of several years and can be subject to uncertain future production levels and sales affecting royalties and other payments. Thus the value of such cases is not fully known at the time OMC approvals are granted.

OMC reports on authorized exports also do not include such values as those associated with repair services or replacement items that may be authorized for export under authority of temporary import licenses which may have been used to return items to the United States for repair.

The Value of Actual Exports Is Understated

OMC provides data on actual export values to Defense Security Assistance Agency (DSAA), which includes the information in its annual reports on foreign military sales. A DSAA official has expressed concern that OMC's data is not verified, current, or compatible with other data in the report. Based on our assessment of the data, we agree.

Actual exports can lag behind approvals by as much as 2 years, since licenses are valid for that period of time, but other factors serve to make the actual export data incomplete. They center around Customs' processing of munitions export licenses and related documents, including Shipper's Export Declarations (SEDs). Customs sends OMC data on actual exports through SEDs indicating individual shipments against licenses and ultimately sends OMC expired licenses. Problems identified by OMC and Customs officials included the following:

Exports were sometimes made without exporters first presenting SEDs for validation and debiting against the export license. Customs officials acknowledged that they do not always catch these. This can occur particularly when the SED does not indicate that the item being shipped is subject to munitions licensing and is improperly marked to indicate authority to ship under less restrictive Commerce Department export authority.

- The process of checking SEDs against export licenses at individual Customs locations and recording exports on the individual licenses was being done manually, and often under time pressures, at the locations we visited. Customs officials acknowledge that their process is subject to errors, but time and resource constraints often do not permit quality control checks.
- OMC officials indicated that expired licenses and SEDs were not received from Customs in a timely manner or at all. An OMC official estimates that tens of thousands of SEDs are never received by OMC and reported receiving licenses 4 to 5 years after they had expired. OMC did not have an ongoing system for tracking licenses to ensure that they were returned and could not provide us with the number of expired but unreturned licenses. In addition, a headquarters Customs official said that OMC has not notified them about any problem concerning the return of SEDs and licenses and that OMC has not specified a time frame for their return.

Shipment values for a given year are subject to change as OMC updates its records with SEDs or returned licenses. However, OMC does not usually update prior years' values in its end-of-year reports on exports it provides to DSAA. OMC updated prior years' export values only at the end of fiscal year 1985 when it updated export values for fiscal years 1983 and 1984. In doing so, the value of exports for fiscal year 1984 increased from $1.6 billion to $3.8 billion, and the value of exports for fiscal year 1983 increased from $2.4 billion to $4.0 billion. OMC cited limited computer resources as a reason for not updating prior years' export values when it provided export data for fiscal year 1986.

Objectives, Scope, and Methodology

We examined the Department of State's munitions export licensing system, focusing on OMC, the group delegated responsibility for licensing munitions exports. Our objective was to determine how well OMC carries out its responsibility to review registrant and export license applications to ensure munitions exports are made in accordance with U.S. foreign policy and national security interests.

Specifically, we examined OMC's licensing activities and procedures, including timeliness and exporter compliance with certain administrative and reporting requirements. Because the documentation associated with licensing reviews was not readily available, we did not examine whether licenses were improperly granted. We also did not examine whether munitions were improperly exported.

We interviewed OMC management officials as well as licensing and compliance staff. We also contacted officials in other State Department offices and other agencies, including the Departments of Commerce and Defense and the U.S. Customs Service, that deal with munitions and other exports. We obtained the views of Customs headquarters staff and field staffs in New York and Los Angeles concerning enforcement and compliance issues related to OMC's overall regulatory role. Additionally, we contacted a limited number of industry representatives for their perceptions of the munitions export licensing process. We also obtained and reviewed pertinent reports, studies, and other documentation available from the various organizations contacted.

In conducting our review, we examined two samples of license applications and other reviews for export approval processed by OMC. These are detailed below.

- We randomly sampled 162 permanent export license applications for more detailed examination. We drew the sample from applications received during the fourth quarter of fiscal year 1986 to help ensure recency of the data while using cases likely to have been completed, i.e., approved or denied.
- We also randomly selected a sample of 1,333 cases out of approximately 49,000 fiscal year 1986 cases (license applications and other reviews) and computed processing time.

Our review was conducted from July 1986 to May 1987. Except for the fourth quarter sample data, we were not able to verify data in OMC's computerized records to source records because of the lack of documentation, the complexity of the system, and the time necessary to perform such an examination. Except for this limitation, our review was conducted in accordance with generally accepted government auditing standards.

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